

***United States Court of Appeals
for the
District of Columbia Circuit***



**TRANSCRIPT OF
RECORD**

BRIEF FOR APPELLANT AND JOINT APPENDIX

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 15,967

386

D. C. TRANSIT SYSTEM, INC., APPELLANT

v.

**PUBLIC UTILITIES COMMISSION OF THE
DISTRICT OF COLUMBIA, APPELLEE**

**Appeal from a Decision of the United States District
Court for the District of Columbia**

*United States Court of Appeals
For the
District of Columbia Circuit*

FILED NOV 1 1960

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QUESTIONS PRESENTED

1. In directing D. C. Transit System, Inc. to credit its depreciation reserve accounts with \$613,661.28 over and above the original cost of certain properties was an accounting order of the Public Utilities Commission of the District of Columbia so unreasonable, arbitrary or capricious as to require that the order be set aside and vacated?

2. In requiring D. C. Transit System, Inc. to credit its depreciation reserve accounts with \$613,661.28 over and above the original cost of certain properties, by transferring said amount from its Earned Surplus account was the accounting order concerned confiscatory and, therefore, unconstitutional?

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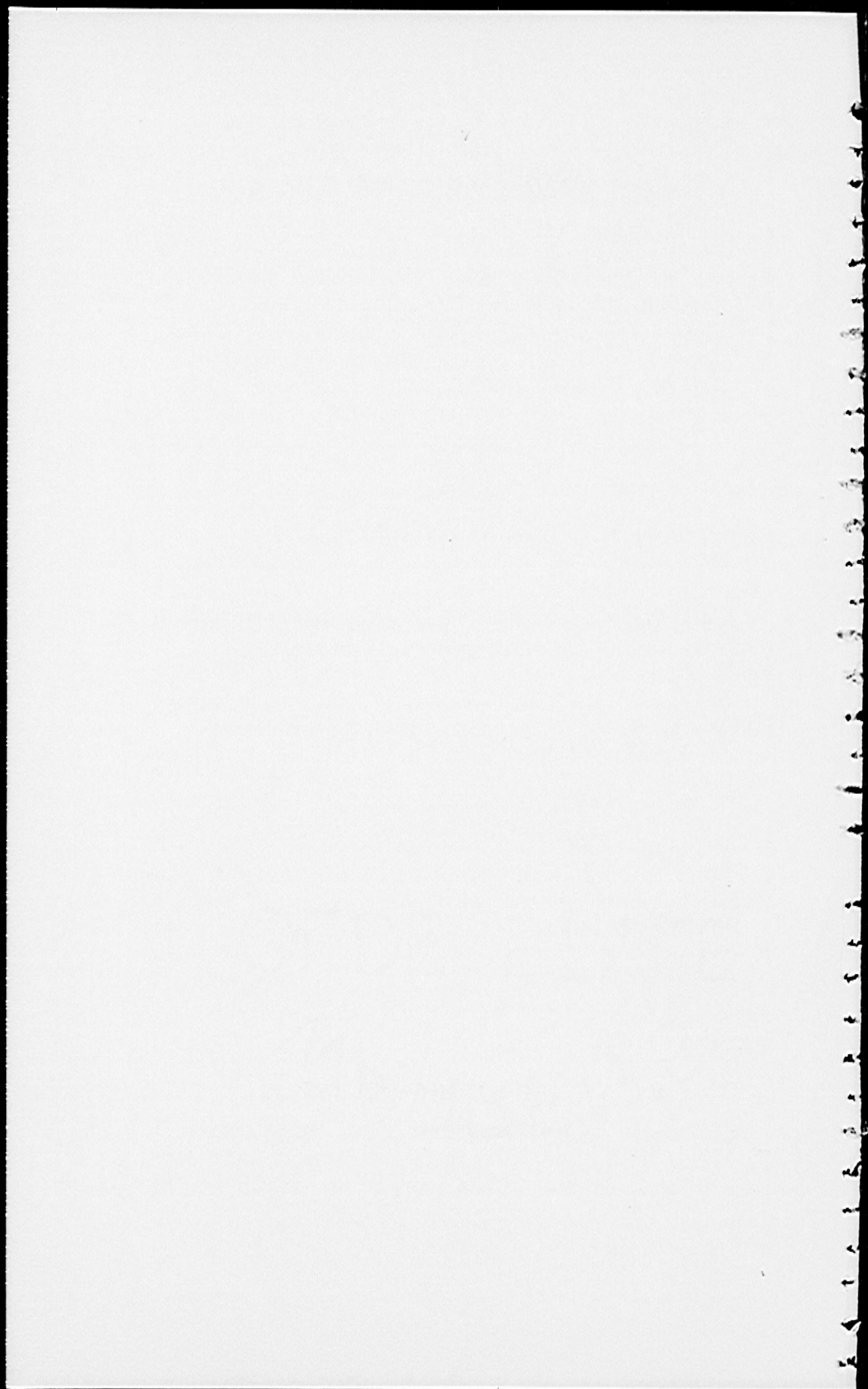
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v.

**PUBLIC UTILITIES COMMISSION OF THE
DISTRICT OF COLUMBIA, APPELLEE**

**Appeal from a Decision of the United States District
Court for the District of Columbia**

BRIEF OF APPELLANT

JURISDICTIONAL STATEMENT

The jurisdiction both of the Court below and of this Court is founded upon Paragraph 65 et seq. of the Act of March 4, 1913 (37 Stat. 974), Section 43-705 et seq., D. C. Code, 1951 Edition. The factual basis of the jurisdiction of the Court below is set forth in Paragraphs I and II of Appellant's Petition of Appeal below filed November 24, 1959 (J.A. 3a).

STATEMENT OF THE CASE

In January, 1959, under threat of condemnation, D. C. Transit System, Inc. (hereinafter "Transit" or "Company") sold certain of its properties, known as its

Fourth Street Shops and Southern Carhouse, to the District of Columbia Redevelopment Land Agency (hereinafter "R.L.A.") for the sum of \$3,320,000. The sales price was the result of negotiations between Transit and R.L.A. in which Transit originally claimed \$3,928,875. In accounting for the proceeds of the sale, the Company credited to its Earned Surplus account all proceeds in excess of the undepreciated original cost of the properties, after certain other adjustments not pertinent to this proceeding.

Immediately prior to the sale, the applicable debit balance in the Company's property account for the properties here concerned¹ was \$1,077,824.06, which figure reflected the original cost of such properties. At that time, the applicable credit balance in the depreciation reserve accounts attributable to the properties was \$613,661.28. Consequently, prior to the sale, the remaining undepreciated original cost of the properties was \$464,162.78 (\$1,077,824.06 less \$613,661.28). At the time of the sale, and in keeping with accepted accounting practice, Transit credited the aforementioned depreciation reserve accounts, out of the proceeds of sale, with \$464,162.78, the amount of the remaining undepreciated cost of the properties. In doing so, the credit balance in the depreciation reserve accounts covering these properties was increased to \$1,077,824.06, the same amount as the debit balance in the properties accounts, representing the original cost of the properties. After thus increasing the credit balance in its depreciation reserve accounts to \$1,077,824.06, the Company wrote-off the two equal accounts by a write-off of the debit balance of \$1,077,824.06 in the properties account and a write-off of the credit balance of \$1,077,824.06 in the depreciation reserve accounts. In this way, the remaining undepreciated original cost of the properties, as

¹ The transaction included the sale of land, buildings and equipment. This appeal relates only to Adjustment Entry No. 1 of the Commission's order dealing with depreciable property.

of the time of sale, was fully recovered out of the proceeds of the sale.

On March 18, 1959, the Public Utilities Commission of the District of Columbia (hereinafter "Commission") addressed a letter to the Company (J.A. 33a) noting Transit's accounting for the proceeds of the sale and requesting information concerning the basis for arriving at the total sales price referred to above. Such data were supplied the Commission by the Company on March 20, 1959 (J.A. 34a). On April 7, 1959, the Commission advised Transit (J.A. 35a) that its staff had questioned the Company's accounting, and noted that the Commission's Uniform System of Accounts provides that with respect to depreciable property any amount received from the sale thereof represents salvage value and should be credited to the depreciation reserve. At the same time (J.A. 35a) the Commission noted that, in this case, to credit the reserve with all of the proceeds of sale of the depreciable property would result in a credit balance in the reserve "somewhat in excess" of the amount required to meet the retirement of the original cost of the property. (In the Discussion and Conclusions in support of the order herein complained of, the Commission stated that application of the Uniform System of Accounts in this instance would result in building the reserves for depreciation to a point where they would contain approximately 80% more than was necessary to retire 100% of the original cost of the properties [J.A. 16a], and concluded that under the circumstances, a departure from the Uniform System of Accounts was warranted [J.A. 16a]). The Commission advised Transit that while its staff recognized the unusual nature of the situation (J.A. 36a), it anticipated that the Company would incur extraordinary property losses in connection with future retirements of property incident to the conversion of Transit's operation from streetcars to buses, which losses were not provided for in the depreciation reserves, and that, in view of this, had proposed

that the net proceeds from the sale of the depreciable property be credited entirely to the depreciation reserve (J.A. 37a). The Commission requested the benefit of Transit's comments on the staff proposal (J.A. 38a).

On June 23, 1959, Transit responded to the Commission's request (J.A. 39a), and indicated the views which had led it to the form of accounting it had employed. Prominent among these, was the view that, as the staff had found, the situation presented was an unusual one (J.A. 39a). The Company felt that a departure from the usual retirement accounting procedures was warranted (J.A. 39a). It was pointed out by the Company that the basis for the Company's allocation of proceeds to its depreciation reserves was a depreciation study conducted by the Commission, and that a conference had been had between Company representatives and representatives of the staff, at which time the staff indicated no disagreement with the basis for Transit's allocation (J.A. 39a). It appeared, therefore, that the only reason for the Commission withholding approval of Transit's accounting lay in the staff's interest in retaining a portion of the proceeds in a reserve to meet future, unknown losses. The Company so advised the Commission (J.A. 40a-41a) and indicated its strenuous objection to the staff's proposal, stating that it regarded as illogical any suggestion which would have the effect of building the depreciation reserves for the properties involved to a point grossly in excess of their original cost (J.A. 40a). The Company asserted that the sale price received was the fair present value of the properties, and that the excess of the proceeds of sale over original cost represented not the appreciation of the buildings, but the decline in the value of the dollar, observing that substantially 30% of its Fourth Street Shop and approximately 50% of its Southern Carhouse properties were built prior to 1915, with the last significant addition to the former being made in 1949 (J.A. 40a). It this con-

nection, Transit directed the Commission's attention to the impact of economic inflation on costs of construction since 1915, and requested that the Commission give its approval to the Company's accounting treatment of the proceeds of the sale.

On September 30, 1959, the Commission promulgated its Order No. 4577 (J.A. 8a), Adjustment Entry No. 1 of which (J.A. 21a) directs the accounting to be made for the proceeds of sale of the depreciable property. This adjustment is the subject of this appeal. At the outset of its Discussion and Conclusions in support of the order, the Commission noted that it had never recognized its Uniform System of Accounts as an inflexible code from which departures in special circumstances cannot be authorized. It agreed with the Company that the circumstances of this case justified such a departure (J.A. 16a). Concerning the extent of departure, the Commission noted that the Company's books reflected accruals of depreciation for the properties involved in the amount of \$613,661.28 (J.A. 16a). (As indicated above, this accrual was based upon an earlier depreciation study and order of the Commission itself.) The Commission admitted that the property has been subject to accruals for depreciation in the past (J.A. 16a), but observed that no provision had ever been made for segregating the reserve by particular units or classes of property (J.A. 16a). No attempt was made to allocate any part of the existing reserve to these properties. Instead, the Commission merely called attention to an alternate proposal of its staff under which, in addition to the \$464,162.78 credited to the reserve by the Company, an amount of \$613,661.28 out of the proceeds should be included in the reserve. The total amount thus proposed to be credited to the reserve out of the proceeds of the sale was \$1,077,824.06, a sum equal to the original cost of the properties sold (J.A. 17a). The Commission accepted this staff proposal, and by Adjustment Entry No. 1 of its

order directed Transit to transfer \$613,661.28 of the proceeds of the sale from its Earned Surplus account to three different accrued depreciation accounts (J.A. 21a). It concluded that such an approach would take into consideration the right of the Company to recover from its customers through depreciation the loss of service value over the life of the property less net salvage realized upon retirement, and, in an effort to explain its refusal to countenance the prior depreciation accruals for these properties, theorized that inasmuch as the net salvage recovered upon retirement in this instance exceeded the original cost of the property, it was established that there was no actual retirement loss over its life (J.A. 17a). In addition, the Commission concluded that it was unable to disassociate the transaction under consideration from certain provisions of Transit's franchise requiring a gradual conversion of its operations from streetcars to buses over a seven-year period from July 24, 1956 (J.A. 18a). It noted a probability that upon future retirements of rail property full provision will not have been made for their depreciation (J.A. 18a), and that under past agreements between Transit and the Commission such losses should be recovered by charges against customers. From this, the Commission concluded that since the customers are to be required to bear the burden of extraordinary retirement losses, they should share, to some extent, in extraordinary retirement gains of the nature here under consideration (J.A. 18a).

The Commission entered its order on September 30, 1959. In due course, Transit filed a petition for reconsideration (J.A. 22a), which the Commission denied (J.A. 43a). Thereafter, the Company filed a petition of appeal in the Court below (J.A. 3a) requesting that the Commission's order be set aside and vacated. The action was heard below on cross-motions of the Commission and the Company for summary judgment (J.A. 25a-27a). On

June 10, 1959 that Court filed its memorandum opinion (J.A. 28a) stating that in its opinion the Commission's order is not unreasonable, arbitrary or capricious. The Court's order granting the Commission's Motion for Summary Judgment and denying Transit's cross-motion was filed on June 24, 1960 (J.A. 28a). Transit's Notice of Appeal was filed in the Court below on July 22, 1960 (J.A. 30a).

STATUTES INVOLVED

Act of March 4, 1913 (37 Stat. 974), § 8:

"Par. 16. That every public utility shall carry a proper and adequate depreciation account. The Commission shall ascertain and determine what are the proper and adequate rates of depreciation of the several classes of property of each public utility. These rates shall be such as will provide the amounts required over and above the expense of maintenance to keep such property in a state of efficiency corresponding to the progress of the industry. Each public utility shall conform its depreciation accounts to such rates so ascertained and determined by the Commission. The Commission may make changes in such rates of depreciation from time to time as it may find to be necessary. The Commission shall also prescribe rules, regulations, and forms of accounts regarding such depreciation which the public utility is required to carry into effect. The Commission shall provide for such depreciation in fixing the rates, tolls, and charges to be paid by the public. All moneys in this fund may be expended in keeping the property of such public utility in repair and good and serviceable condition for the use to which it is devoted, or invested, and, if invested, the income from the investments shall also be carried in the depreciation fund. This fund and the proceeds thereof shall be used for no other purpose than as provided in this paragraph, unless with the consent and by order of the Commission." D.C. Code, Sec. 43-315 (1951 edition).

"Par. 65. * * * Any public utility, or any other person or corporation affected by any final order or decision of the commission, * * *, may, * * *, file with the Clerk of the District Court of the United States for the District of Columbia, a petition of appeal setting forth the reasons for such appeal and the relief sought; * * *"

"Any party, including said commission, may appeal from the order or decree of said Court to the Court of Appeals of the District of Columbia, which shall thereupon have and take jurisdiction in every such appeal. * * *" D. C. Code, Sec. 43-705 (1951 edition).

"Par. 66. In the determination of any appeal from an order or decision of the Commission the review by the Court shall be limited to questions of law, including constitutional questions; and the findings of fact by the commission shall be conclusive unless it shall appear that such findings of the commission are unreasonable, arbitrary or capricious." D.C. Code, Sec. 43-706 (1951 edition).

Public Law 757, 84th Cong. (70 Stat. 598):

"Sec. 7. The Corporation shall be obligated to initiate and carry out a plan of gradual conversion of its street railway operations to bus operations within seven years from the date of the enactment of this Act upon terms and conditions prescribed by the Commission, with such regard as is reasonably possible when appropriate to the highway development plans of the District of Columbia and the economies implicit in coordinating the Corporation's track removal program with such plans; except that upon good and sufficient cause shown the Commission may in its discretion extend beyond seven years, the period for carrying out such conversion. * * *"

Public Law 86-669, 86th Cong., approved July 14, 1960:

"Sec. 204. The Agency—

(b) Shall, in the preparation of the Transit Development Program, give special consideration to:

(1) Expanded use of existing facilities and services, including expanded use and development of

existing railroad lines into the District of Columbia, and coordinated and efficient transit service across jurisdictional boundaries and between areas served by different companies: Provided, That the Public Utilities Commission of the District of Columbia, before granting its approval to any further conversion by the D. C. Transit System, Inc., of street railway operations to bus operations as provided in section 7 of the Act of July 24, 1956 (70 Stat. 598), shall consult with the Agency on the possible use of street railway facilities and equipment in the Transit Development Program. The Commission may withhold its approval of such conversion and require the preservation of equipment and facilities already withdrawn from service if it finds that there is a substantial possibility that the Transit Development Program will provide for the continued use of street railway facilities and equipment."

STATEMENT OF POINTS

1. In requiring appellant to credit its depreciation reserve accounts with \$613,661.28 over and above the original cost of the properties here involved, Adjustment Entry No. 1 of Order No. 4577 of the appellee Commission was unreasonable, arbitrary and capricious within the meaning of Section 8, Paragraph 66 of the Act of March 4, 1913 (37 Stat. 794) supra; Section 43-706, D.C. Code, 1951 Edition. The failure of the Court below to so hold was error.
2. In concluding that there was no loss of service value over the life of the properties here involved, Order No. 4577 of the appellee Commission was unreasonable, arbitrary and capricious within the meaning of the aforementioned statute, and the failure of the Court below so to hold was error.
3. In relating the action directed to be taken by appellant under Adjustment Entry No. 1 to the conversion requirements of Section 7 of Public Law 757, 84th Cong.

(70 Stat. 598) supra, Order No. 4577 was unreasonable, arbitrary and capricious within the meaning of the aforementioned statute, and was without support in the evidence. The failure of the Court below so to hold was error.

4. In requiring appellant to transfer \$613,661.28 from its Earned Surplus account to accrued depreciation accounts, Adjustment Entry No. 1 of Order No. 4577 of the appellee Commission was confiscatory and, therefore, unconstitutional. The failure of the Court below so to hold was error.

SUMMARY OF ARGUMENT

D. C. Transit's first contention on this appeal is that Adjustment Entry No. 1 of the Commission's Order No. 4577 is so unreasonable, arbitrary and capricious as to require that it be set aside and vacated. In this connection, it is the Company's position that its accounting for the proceeds of sale of the depreciable properties involved is in strict accordance with correct accounting principles, and that the accounting ordered by the Commission is so contrary to such principles as to represent reversible error on the part of the Commission. Transit insists that since its accounting reflects past depreciation accruals for the properties in accordance with the Commission's prior depreciation orders, and credits the reserves concerned in accordance with the Commission's latest depreciation study, the order of the Commission constitutes an unreasonable, arbitrary and capricious disregard of such past accruals and of the Commission's own depreciation study. It is Transit's position that the Commission's conclusion that merely because the proceeds of sale of the properties exceeded their original cost there was no retirement loss over the life of the properties is incomprehensible, and represents an utter disregard of the facts and of economic realities.

Depreciation is a function of the use of depreciable property. In this instance, the Commission admits that reserves have been accrued against these properties over the years. The Commission's conclusion also reflects a complete disregard of the impact of inflation on the value of the dollar. It chose to ignore the great disparity between construction costs at the time substantial portions of the properties were constructed and such costs today. Transit contends that it was unreasonable so to do.

Finally, with respect to its first contention, it is the Company's position that in relating the accounting transaction before it in this case to the conversion requirements of Transit's franchise the Commission arbitrarily stepped beyond the scope of subject matter before it. In so doing, it confused two totally unrelated subjects. Transit contends that the sole matter before the Commission was the matter of accounting for the proceeds of sale of two particular properties. It had nothing whatsoever to do with future probabilities respecting other dissimilar properties. It is the Company's position that the Commission's action constituted an entirely illogical offsetting of present known credits against unknown future losses which may, in fact, never materialize, and such action is accordingly without support in the evidence.

Transit's second contention is that in directing the Company to credit its depreciation reserves with \$613,661.28 over and above the original cost of certain properties, by a transfer of that amount from its Earned Surplus account, the order of the Commission is confiscatory and unconstitutional. In effect, the order deprives the Company of the benefit of past accruals for depreciation with respect to the properties involved, and jeopardizes its settled right to fair and reasonable depreciation accruals on other of its properties in the future. In addition, by directing the transfer of this large credit from Transit's Earned Surplus account to depreciation

reserve accounts, the order complained of restricts the Company's freedom in its application of the funds involved. As part of depreciation reserves the funds may, unless the Commission orders otherwise, be drawn against only for the maintenance and replacement of property. On the other hand, as surplus they would be available for these and such other purposes as management, in its sound judgment, may deem necessary and advantageous to the Company.

It is Transit's position that in depriving it of its past depreciation accruals, in jeopardizing its right to fair and reasonable depreciation charges against other properties in the future, and in arbitrarily restricting its full use of the funds here involved, the order complained of is confiscatory and unconstitutional.

ARGUMENT

POINT I

In Requiring Transit to Credit Its Depreciation Reserve Accounts With \$613,661.28 Over and Above the Original Cost of the Properties, Adjustment Entry No. 1 Is Unreasonable, Arbitrary and Capricious.

The record on this appeal reflects that the effect of Adjustment Entry No. 1 of the Commission's order is to compel Transit to credit its depreciation reserve accounts with \$613,661.28 over and above the original cost of the properties involved. There is no dispute over the original cost of the properties, \$1,077,824.06. Similarly, there is no question that over the life of the properties depreciation reserves have been accrued. Transit's statement that its accrued reserve attributable to the properties concerned amounts to \$613,661.28 stands unchallenged by any other figure, and the basis for the Company's calculation of this accrual has not been questioned. The Commission's only justification for the adjustment it has

ordered are its conclusions, dealt with in Points II and III below, that because the proceeds of the sale of the properties exceeded their original cost there was no actual retirement loss over their service lives, and that this transaction is related to the conversion requirements of the Company's franchise.

Transit respectfully submits that this order denotes a complete and utter disregard by the Commission of its prior depreciation accounting experience with these properties, and its orders and studies affecting them. In this connection, the Court's attention is directed to Paragraph 16 of Section 8 of the Act of March 4, 1913, Section 43-315, D.C. Code, 1951 Edition, *supra*, the statute which created the Commission. It provides that every public utility shall carry a proper and adequate depreciation account, and directs the Commission to ascertain and determine proper and adequate rates of depreciation for the several classes of property of each such utility. Over the years there has been compliance with these directions. Depreciation reserve accounts have been established and maintained, and the Commission has dictated the rates for accruals against different classes of property. Up to the time of its sale by the Company the property involved in this case was continuously covered by appropriate accounts, and by order of the Commission, at rates prescribed by the Commission, it was the object of substantial depreciation accruals. In 1952, the Commission conducted a thorough-going depreciation study of the Company's properties, including the property involved here. That study revealed that accruals with respect to these properties then amounted to approximately \$407,000, and, as evidenced by the record before the Commission and the Court below, Transit predicated its accounting on this study and on depreciation rates established by the Commission.

It is generally held that orders of public service commissions affecting public utilities in the transaction of

their business or as to their property rights may be challenged in the courts if they are without evidence to support them and are merely arbitrary edicts and are unjust, arbitrary and unreasonable when applied to the facts. 43 *Am. Jur., Public Utilities and Services, Section 227* citing *Norwegian Nitrogen Products Co. v. United States*, 288 U.S. 294, 53 Sup. Ct. 350, 77 L. Ed. 796. See also, Paragraph 66 of Section 8 of the Act of March 4, 1913, *supra*. Transit submits that the Commission's utter disregard of admitted facts, the facts of substantial past accruals of depreciation reserves for the property involved here and the fact that the Commission's own prior study reflected such reserves, constrains the conclusion that the adjustment complained of is arbitrary and unreasonable. Webster's International Dictionary, Second Unabridged Edition, defines the term "arbitrary" as descriptive of actions which are unreasoned and are taken without regard for circumstances. This is precisely what has occurred here. The Commission has ignored the past.

In *American Telephone & Telegraph Co. v. United States*, 14 F. Supp. 121, affirmed 299 U.S. 232, 57 Sup. Ct. 170, 81 L. Ed. 142, a statutory three judge court had before it the complaints of numerous telephone utilities respecting accounts prescribed by the Federal Communications Commission. Among the items complained of was the refusal of the Commission to permit the accrual of depreciation reserves on property held for future use, and a requirement that with respect to certain property acquisitions the companies were compelled, in addition to the usual accounting for purchases, to record a portion of such transactions twice. With respect to the former point, the Court held that to bar depreciation accruals would be unreasonable. Transit contends that Adjustment Entry No. 1 has the effect of barring depreciation of the properties involved in an *ex post facto* fashion, and is, therefore, unreasonable. On the latter point, the

Court found that the accounting ordered was a double recording of particular transactions which had the effect of swelling the asset and liabilities accounts by fictitious entries. It held that to require such double accounting was unreasonable. In the present case, Transit would be compelled to duplicate its past accruals for depreciation of the property involved, and the reserves attributable to the property would be swollen to a point where they would contain approximately 50.47% more than is required to retire 100% of their original cost.

In summary on this point, Transit respectfully contends that Adjustment Entry No. 1 of the Commission's order completely ignores all past depreciation accounting for the properties involved, disregards the Commission's own orders and studies in this regard, compels a gross over-depreciation of the properties, and is, therefore, so unreasonable, arbitrary and capricious as to require that it be set aside and vacated.

POINT II

In Concluding That There Was No Loss of Service Value Over the Life of the Properties Order No. 4577 Is Unreasonable, Arbitrary, and Capricious.

In ordering Transit to credit \$613,661.28 over and above the original cost to accrued depreciation reserves for the properties involved here, the Commission theorizes that merely because the proceeds of sale exceeded the original cost of the properties there was no actual retirement loss over their lives. It was on this theory that the Commission ignored all prior accruals against these properties and its own prior depreciation study and orders. Transit respectfully submits that this theory is patently erroneous, and in asserting it in support of the present order the Commission has acted unreasonably, arbitrarily and capriciously.

It is axiomatic that depreciation is a function of the use of depreciable property over its lifetime. It is the loss, not restored by current maintenance, which is due to all factors causing the ultimate retirement of the property. The factors to be considered embrace wear and tear attributable to use and the effect of all physical forces on the property causing decay, inadequacy and obsolescence. *Lindheimer v. Illinois Bell Telephone Co.*, 292 U.S. 151, 54 Sup. Ct. 658, 78 L. Ed. 1182. The record in this case reveals that approximately 30% of one of the properties involved was constructed prior to 1915, the latest addition of any importance having been made in 1949, and that approximately one-half of the other property in question was built prior to 1915. There is no question that throughout the years these properties were continuously used by Transit in its operations. There is, likewise, no question that over the years the properties have been subject to all the forces, in addition to that represented by their constant use, which contribute to the decay, inadequacy, and obsolescence of property generally. Depreciation is an unavoidable fact of life. Transit contends that the Commission's theory is, to say the least, untenable. It is completely at odds with the fact that over their lifetimes the properties involved did suffer an inevitable, gradual exhaustion. It is, therefore, an unreasonable and arbitrary conclusion.

Two other features of this theory warrant attention. In the first place, it rests on the simple conclusion that merely because the proceeds of sale of these properties exceeded their original cost there must not have been any retirement loss over their lifetimes. Transit contends that such a conclusion evades economic reality. It completely ignores the fact that the sale price of the properties necessarily reflected the inflation in the reproduction cost of the properties between their dates of acquisition (in some cases prior to 1915) and the date of their sale in

January, 1959. The record herein reveals that the sale price in January, 1959 was based upon an appraisal of reproduction cost less accrued depreciation at that time (J.A. 9a). That appraisal established the then reproduction cost of these properties at \$2,071,240,² a figure considerably higher than the original cost because of the intervening inflation in construction costs between 1915 and 1959. The record reveals that in 1915 the construction cost index was 34, and that by 1956 it had increased to 154 (J.A. 40a). At the time of sale, therefore, the reproduction costs were more than four times what they had been when these properties were originally acquired. The appraisal referred to above was a net appraisal figure, i.e., reproduction cost less accrued depreciation. The effect of inflation since 1915 has been so great that the cost of reproducing the properties in January, 1959, computed at reproduction cost less depreciation over their service lives, was an amount which, even after such depreciation, still exceeded original cost. Far from indicating that there was no actual retirement loss over the service life of the properties, the appraisal figure portrays reproduction cost after giving effect to the allocable retirement loss actually experienced. Had there been no actual retirement loss, the appraisal figure would have been even higher than the net figure of \$2,071,240.

Transit contends that the foregoing circumstances cannot be ignored. It is a gross over-simplification to conclude, as the Commission has done, that merely because the number of dollars received for the properties in 1959 exceeded the number required to purchase the same properties so many years ago, no retirement loss has occurred. The impact of inflation on the value of the dollar has been pronounced, and Transit submits that the difference between a 1959 sales price and original cost prices dating

² The price actually received, \$1,921,240 was the result of negotiations between Transit and the purchaser.

back to the early years of the century is not a measure of retirement loss. In so concluding, the Commission has acted arbitrarily, unreasonably and capriciously.

Past depreciation accruals with respect to these properties were allowed for in the negotiated price. The Company should not be penalized by this refusal of the Commission to recognize such depreciation in accounting for the proceeds of the sale. In *Chicopee Manufacturing Company, et al. v. Public Service Company*, (1953), 93 A.2d 820, 98 P.U.R. (NS) 187, 195, the New Hampshire Supreme Court considered certain appeals from a decision of the State Public Utilities Commission. Among the questions before the Court was one relating to a floating electric generating plant known as the "Jacona" which had been seized by the United States Government for use in World War II. The price paid by the government exceeded the depreciated cost to the Company by some \$418,570. In disposing of that action, the Court held that inflationary forces and the war emergency had brought about the profit involved and that such considerations do not provide a basis for reaccounting for depreciation. There can be no doubt that in compelling the addition of more than \$600,000 to the depreciation reserves covering the properties here involved constitutes a reaccounting, to the detriment of the Company, for a like amount of reserves already on its books. Transit contends that the unavoidable impact of economic inflation is a factor which the Commission cannot reasonably ignore, and that its influence with respect to the value of the properties involved should not be permitted to occasion their gross over-depreciation.

Finally, on this point, Transit deems it appropriate to point out that the Commission's approach to the transaction involved here is a departure from its past and present standards of property valuation. In the past, this Commission's orders and studies relating to deprecia-

tion have been predicated on original cost. Throughout the service life of the properties involved here reserves were accrued pursuant to rates founded on such cost. Adjustment Entry No. 1, however, recognizes replacement cost, a basis for depreciation not heretofore adopted by the Commission. See *Spiegel v. Public Utilities Commission*, 101 U.S. App. D.C. 93, 247 F.2d 84. Here, the Commission is recognizing replacement cost on the disposal of property, but adhering to original cost depreciation for property continuing in service. It is the Company's position that such treatment is inconsistent and unreasonable. Since replacement cost depreciation was not allowed during the service life of these properties, the Commission cannot now restate their depreciation reserves on a replacement cost basis, without depriving the Company of property. In addition, Transit feels that if the present order is permitted to stand, the additional accrual to depreciation reserves required thereby will adversely affect the Company's position in future rate making proceedings. The Company respectfully submits that the Commission acts arbitrarily in relying upon fair value to reach its result in this instance, while refusing to recognize such value in regulating its depreciation accruals generally.

POINT III

In Relating Its Order to the Conversion Requirements of Transit's Franchise the Commission Acted Unreasonably, Arbitrarily, Capriciously, and Without Support in the Record.

As additional support for its order, the Commission relies upon certain unrelated matters. It argues that Adjustment Entry No. 1 is justified on the completely unsupported theory that the sale of the properties involved here was related to the provisions of Section 7 of Public Law 757, 84th Cong. (70 Stat. 598) *supra*, Transit's franchise, which requires the Company to con-

vert all of its rail properties to bus operation by the end of 1963. In this connection, the Commission argues that it knows that retirement losses are "probable" when the abandonment of rail property takes place. The record, however, is bereft of any evidence bearing upon the magnitude of such alleged prospective losses, and it is Transit's position that this order cannot be sustained on the basis of mere probabilities. It is, in this respect, merely a general opinion of the Commission unsupported by findings of fact based on substantial evidence. *Washington Gas Light Company v. Public Utilities Commission*, 55 F. Supp. 627, *Spiegel v. Public Utilities Commission*, 96 U.S. App. D.C. 307, 226 F.2d 29, 33, *Washington Gas Light Company v. Baker*, 104 U.S. App. D.C. 321, 188 F.2d 11, 23, cert. denied 340 U.S. 952, 95 L. Ed. 686. The sole support of record for the Commission's action here is its opinion that since Transit's customers must bear the expense of extraordinary losses associated with "probable" future conversion, they are entitled to share in the benefits of extraordinary gains of the nature here under consideration. In this connection, it is necessary to observe that any "probable" future burden imposed on customers would be measured by the original cost of properties retired as a result of conversion. Here, however, the Commission seeks to confer a benefit measured in terms of 1959 dollars, or replacement cost. It is Transit's position that it is inconsistent, arbitrary, and unreasonable to measure burdens one way and benefits another.

Transit further contends that the subject matter before the Commission in this case is entirely unrelated to Section 7 of its franchise, *supra*. This case relates to the proceeds of sale of specific properties. It relates to a consummated transaction which was induced by factors completely foreign to any franchise requirement. The threatened condemnation of the properties involved here

was never even contemplated by the franchise or its authors. The issue before the Court in this case is whether D. C. Transit is to be denied the benefit of its proper accounting for the proceeds of a particular sale of specific property. The issue is not what may or may not be necessary with respect to other, perhaps dissimilar, property at some unknown future time. In this connection, the Court's attention is invited to Section 204 (b)(1) of Public Law 86-669, 86th Cong., supra, which was approved July 14, 1960, following the hearing in the Court below. This legislation creates a temporary National Capital Transportation Agency. It provides that before granting its approval to any further conversion by Transit of its rail facilities to bus operations as called for by Section 7 of the franchise, the Commission shall consult with the new agency on the possible use of the Company's existing rail facilities and equipment in the Transportation Development Program described elsewhere in the Act. It provides that the Commission may withhold its approval of further conversion and may require the preservation of equipment and facilities of the Company already withdrawn from service pursuant to conversion if it finds a substantial possibility that the new program will provide for the continued use of such rail facilities and equipment. Certainly, this development illustrates the uncertainty surrounding all questions regarding future conversions. It renders even more conjectural the basis relied upon by the Commission to justify its action in this proceeding. In these circumstances, future retirement losses due to conversion can hardly be deemed a present probability.

Transit cannot stress enough its conviction that the sole question here is the proper accounting for the proceeds of the property it has sold. It contends that in treating this transaction as related to the completely separate, distinct, and highly uncertain prospects of future con-

version, the Commission has ordered an illogical offsetting of known credits against future unknown losses, and that in so doing has acted unreasonably, arbitrarily and capriciously.

POINT IV

In Requiring Transit to Transfer \$613,661.28 From Its Earned Surplus Account to Accrued Depreciation, Adjustment Entry No. 1 Is Unconstitutional.

The confiscatory nature of Adjustment Entry No. 1 of the Commission's order is evident when one analyzes the results achieved by the entry. Its first effect is to compel the removal from the Company's retained or undistributed income of \$613,661.28. In so doing, it removes the funds from the full management and control of Transit's responsible corporate officials. It severely limits the exercise of their judgment with respect to the application of the funds in the best interests of the Company's future progress and its stockholders. As additions to depreciation reserves, Paragraph 16, Section 8 of the Act of March 4, 1913, *supra*, restricts the use of these funds to maintenance and replacement of property unless the Commission consents to or orders some other application. Under normal circumstances, Transit would have no argument with this authority over depreciation reserves, but in this case, where the reserve involved constitutes an arbitrary gross over-depreciation of specific properties, it contends that to so restrict the Company in its use of the funds involved is to interfere beyond regulatory warrant with proper exercisable discretion in a matter solely within the responsibility of Transit's Management, and is tantamount to a deprivation of the Company's property without due process of law. In *State of Missouri ex rel. S.W. Bell T. Co. v. Public Service Commission*, 262 U.S. 276, 289, 43 Sup. Ct. 544, 67 L. Ed. 981, 985 the Supreme Court of the United States said:

" * * * It must never be forgotten that, while the state may regulate with a view to enforcing reasonable rates and charges, it is not the owner of the property of public utilities companies and is not clothed with the general power of management incident to ownership. The applicable general rule is well-expressed in *State Public Utilities Commission ex rel. Springfield v. Springfield Gas & E. Co.*, 291 Ill. 209, 234, P.U.R. 1920 C 640, 125 N.E. 891: 'The Commission is not the financial manager of the corporation, and it is not empowered to substitute its judgment for that of the directors of the corporation; nor can it ignore items charged by the utility as operating expenses unless there is an abuse of discretion in that regard by the corporate officers.' "

and in *United R. Electric Co. v. West*, 280 U.S. 234, 249, 50 Sup. Ct. 123, 74 L. Ed. 390, overruled on other grounds in 320 U.S. 591, 607, 64 Sup. Ct. 290, 88 L. Ed. 333, 347, the Court said:

" * * * the fundamental principle to be observed is that the property of a public utility, although devoted to the public service and impressed with a public interest, is still private property; and neither the corpus of that property *nor the use thereof* constitutionally can be taken for a compulsory price which falls below the measure of just compensation. One is confiscation no less than the other." (Emphasis supplied.)

See also: *Stone v. Farmers Loan & Trust Co.*, 116 U.S. 307, 6 Sup. Ct. 334, 29 L. Ed. 636; *Smyth v. Ames*, 169 U.S. 466, 18 Sup. Ct. 418, 42 L. Ed. 819, *Chicago M. & St. P. R. Co. v. Minnesota ex rel. Railroad & Warehouse Commission*, 134 U.S. 418, 10 Sup. Ct. 462, 33 L. Ed. 462, *Re Minnesota Rate Cases*, 230 U.S. 352, 33 Sup. Ct. 729, 57 L. Ed. 1511. In being denied the full and free use of the \$613,661.28 involved here, Transit's position is that it has been unconstitutionally deprived of a substantial portion of its property.

In addition, the Company contends that the necessary result of Adjustment Entry No. 1 is to deprive Transit of the benefit of all past accruals for depreciation with respect to the properties concerned. The law is well-settled that any action which is calculated to deprive a utility of fair and reasonable depreciation expenses is an unconstitutional deprivation of its property. *Lindheimer v. Illinois Bell Telephone Company*, supra, *Knoxville v. Knoxville Water Co.*, 212 U.S. 1, 29 Sup. Ct. 148, 53 L. Ed. 371, *Washington Gas Light Co. v. Baker*, 104 U.S. App. D.C. 321, 188 F. 2d 11, cert. denied 340 U.S. 952, 95 L. Ed. 686. Here, the Commission has totally ignored all past depreciation accruals, and one consequence of its refusal to countenance them is an invasion of surplus, in the amount of \$613,661.28, to the substantial detriment of the Company.

There is another, less obvious, result of the Commission's action. In requiring the over-depreciation of these properties, Transit's right to fair and reasonable depreciation expenses in respect to its remaining property is placed in jeopardy. To increase such reserves is to diminish, pro tanto, the allowance of future depreciation charges. Consequently, Transit feels that its right to fair and reasonable depreciation expenses on its remaining property is imperiled by the Commission's action in this case, and that any action of the Commission which either denies the Company its right to past depreciation accruals, or jeopardizes its right to fair and reasonable accruals in the future is a deprivation of property without due process of law and is unconstitutional. *Lindheimer v. Illinois Bell Telephone Company*, supra, *Knoxville v. Knoxville Water Co.*, supra, *Washington Gas Light Co. v. Baker*, supra.

CONCLUSION

For the reasons stated above, D. C. Transit respectfully prays that this Court vacate and set aside Adjustment Entry No. 1 of the Commission's Order No. 4577.

Respectfully submitted,

/s/ Harvey M. Spear
HARVEY M. SPEAR

/s/ Owen J. Malone
OWEN J. MALONE
3600 M Street, N.W.
Washington 7, D. C.
Attorneys for Appellant

Washington, D.C.

Dated: November 1, 1960

CERTIFICATE OF SERVICE

A copy of the foregoing Brief for Appellant was served on George F. Donnella, Esquire, Attorney for the Public Utilities Commission of the District of Columbia, at said Attorney's office, District Building, Washington 4, D. C., this 1st day of November, 1960.

OWEN J. MALONE

APPENDIX

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CIVIL DOCKET

UNITED STATES DISTRICT COURT FOR THE
DISTRICT OF COLUMBIA

Proceedings 3306-59

Nov. 24, 1959 Complaint, appearance Exhibits A & B
filed

Nov. 24, 1959 Summons, copies (—) and copies (—) of
complaint issued

Nov. 24, 1959 Certificate of Service filed

Dec. 11, 1959 Motion of deft to dismiss appeal or for
summary judgment, P & A, c/m 12-11-59 M.C. 12-11-59
Appearance of Chester H. Gray & George F. Don-
nella, & Exhibit (Certification & record #3306)

Dec. 18, 1959 Appearance of Owen J. Malone as co-
counsel for pltff. filed

Dec. 18, 1959 Stipulation of counsel extending time in
which to answer defts motion to dismiss to 1-7-60
filed

1960

Jan. 8, 1960 Stipulation extending time for pltff to
answer motion to dismiss to and including 1-21-60
(M/N) filed

Jan. 21, 1960 Stipulation extending time for pltff to
reply to motion to dismiss to and including 2-11-60
(M/N) filed

Feb. 10, 1960 Stipulation of counsel extending time for
pltffs to reply to deft's motion to dismiss per counsel
filed

- Feb. 26, 1960 Stipulation extending time for plttf to
reply to and including 3-25-60 filed
- March 28, 1960 Stipulation extending time until 4-1-60
for plttf to reply to deft's motion to dismiss; (M/N)
filed
- March 31, 1960 Cross motion of plttf for summary judg-
ment; P & A in support & in opposition to defts
motion for summary judgment; c/m 3-31-60; M.C.
3-31-60 filed
- June 2, 1960 Motion to dismiss or for summary judgment
& cross-motion for summary judgment; both motions
argued and taken under advisement (Rep. by E.
Romig) (N) McGarraghy, J.
- June 10, 1960 Memorandum of opinion granting motion
of respondent for summary judgment and denying
cross-motion of petitioner for summary judgment (N)
McGarraghy, J.
- June 24, 1960 Order granting motion of Public Utilities
Commission for summary judgment; dismissing peti-
tion of appeal; affirming Order No. 4577 of Public
Utilities Commission of the District of Columbia dated
Sept. 30, 1959; and denying cross-motion of petitioner
for summary judgment (N) McGarraghy, J.
- July 22, 1960 Notice of plttf of appeal (copy mailed to
deft) filed
- July 22, 1960 Deposit for costs by Harvey M. Spear for
plttf \$5.00
- July 22, 1960 Cost bond on appeal in the sum of \$250.00
with American Casualty Company of Reading, Penn-
sylvania approved & filed

PETITION

(Filed November 24, 1959)

UNITED STATES DISTRICT COURT FOR THE
DISTRICT OF COLUMBIA

Civil Action No. 3306-59

D. C. TRANSIT SYSTEM, INC. (a District of Columbia
corporation), 3600 M Street, N.W., Washington 7, D. C.,
PETITIONER

-against-

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF
COLUMBIA, District Building, 14th and E Streets, N.W.,
Washington, D. C., RESPONDENT

Petition of Appeal

Comes now petitioner, D. C. Transit System, Inc. (a District of Columbia corporation), by its attorney, Harvey M. Spear, pursuant to Public Law 757, 84th Cong., 2d Sess., 70 Stat. 598 (hereinafter referred to as the "franchise") and pursuant to Paragraph 65, Section 8, Chapter 150, Act of March 4, 1913, 37 Stat. 974, as amended (D. C. Code, Title 43, Section 705), and respectfully petitions this Court as follows:

I. Petitioner, D. C. Transit System, Inc., is a validly existing corporation organized under the laws of the District of Columbia on July 9, 1956. Petitioner is the corporation referred to in the franchise, described above. Since August 15, 1956, petitioner has owned and operated the transit system of the District of Columbia and adjacent areas pursuant to its franchise and the laws of the District of Columbia.

II. Respondent, Public Utilities Commission of the District of Columbia is a statutory agency created by the Act of March 4, 1913, 37 Stat. 974, as amended (D. C. Code, Title 43, Section 101).

III. On January 16, 1959, petitioner sold, under threat of condemnation, certain land and buildings located in Southwest Washington known as "Fourth Street Shops" and "Southern Car House" to the District of Columbia Redevelopment Land Agency for a total consideration of \$3,320,000. The excess of the net proceeds over the computed net depreciated cost of the properties sold amounted to \$2,181,363.08, which amount petitioner treated as profit from the sale and credited to its Earned Surplus account.

IV. On September 30, 1959, respondent entered its Order No. 4577 in which, among other changes, respondent ordered petitioner to transfer \$613,661.28 from its Earned Surplus account to three different Accrued Depreciation accounts. A copy of Order No. 4577 is attached hereto and incorporated herein by reference as Exhibit "A".

V. In its Order No. 4577, respondent found and concluded that petitioner was contending that the receipt by petitioner from the sale of the depreciable property of approximately \$837,000 more than the original cost of such property was such an abnormal occurrence that special accounting treatment was justified.

VI. In its Order No. 4577, respondent found and concluded that since the net salvage value recovered from the sale of the property exceeded the original cost thereof, it was thereby established that there was no actual retirement loss over the life of such property.

VII. In its Order No. 4577, respondent found and concluded that the sale of the property was related to the imminent retirement of all rail property under the conversion mandate of Section 7 of petitioner's franchise.

VIII. In its Order No. 4577, respondent found and concluded that the alternate accounting proposal of respondent's staff with respect to the accounting treatment to be accorded the proceeds from the sale of the depreci-

able property provided an equitable solution and maintained a fair balance between the interests of the public and those of petitioner's investors.

IX. On October 30, 1959, petitioner duly filed with respondent its Petition for Reconsideration of respondent's Order No. 4577 dated September 30, 1959. A copy of the petitioner's Petition for Reconsideration filed with respondent October 30, 1959 is attached hereto and incorporated herein by reference as Exhibit "B".

X. On November 12, 1959, respondent entered its Order No. 4587 denying the Petition for Reconsideration filed by petitioner on October 30, 1959.

XI. Respondent erred in its Order No. 4577 dated September 30, 1959 in finding and concluding that petitioner was contending that the receipt by petitioner from the sale of the depreciable property of approximately \$837,000 more than the original cost of such property was such an abnormal occurrence that special accounting treatment was justified, in that petitioner did not so contend.

XII. Respondent erred in its Order No. 4577 dated September 30, 1959 in finding and concluding that since the net salvage value recovered from the sale of the property exceeded the original cost thereof, it was thereby established that there was no actual retirement loss over the life of such property, in that such result was not thereby established.

XIII. Respondent erred in its Order No. 4577 dated September 30, 1959 in finding and concluding that the sale of the property was related to the imminent retirement of all rail property under the conversion mandate of Section 7 of petitioner's franchise, in that the sale was not so related to such imminent retirement.

XIV. Respondent erred in its Order No. 4577 dated September 30, 1959 in finding and concluding that the

alternate accounting proposal of respondent's staff with respect to the accounting treatment to be accorded the proceeds from the sale of the depreciable property provided an equitable solution and maintained a fair balance between the interests of the public and those of petitioners' investors, in that such alternate accounting proposal did not provide an equitable solution or maintain a fair balance between the interests of the public and those of petitioner's investors.

XV. Respondent erred in its Order No. 4577 dated September 30, 1959 in ordering petitioner to transfer \$613,661.28 from its Earned Surplus account to three different Accrued Depreciation accounts, in that such transfer would constitute an erroneous accounting entry.

XVI. Respondent erred in its Order No. 4587 dated November 12, 1959 in denying petitioner's Petition for Reconsideration filed with respondent on October 30, 1959 (Exhibit "B"), in that the Petition for Reconsideration should have been granted.

WHEREFORE, petitioner respectfully prays that this Court:

A. Vacate and set aside respondent's Order No. 4577 dated September 30, 1959 and respondent's Order No. 4587 dated November 12, 1959.

B. Grant such other, further and alternative relief as to this Court may seem just and proper.

Respectfully submitted,

/s/ Harvey M. Spear
Harvey M. Spear
Attorney for Petitioner
3600 M Street, N.W.
Washington 7, D. C.

Dated: Washington, D. C.
November 24, 1959

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CERTIFICATE OF SERVICE

It is hereby certified that a copy of the Petition of Appeal from Orders Nos. 4577 and 4587 herein was this date served upon the Public Utilities Commission of the District of Columbia by the delivery and filing of a copy thereof at the Office of Norman B. Belt, Executive Secretary, District Building, 14th and E Streets, N. W., Washington, D. C.

/s/ Harvey M. Spear
Harvey M. Spear
Attorney for Petitioner
3600 M Street, N.W.
Washington 7, D. C.

Dated: Washington, D. C.
November 24, 1959

EXHIBIT A, ANNEXED TO PETITION

*Opinion and Order of the Commission*PUBLIC UTILITIES COMMISSION OF THE
DISTRICT OF COLUMBIA

Order No. 4577

September 30, 1959

P. U. C. No. 3574/16

In the Matter of
Accounting for Proceeds from Sale by D. C.
TRANSIT SYSTEM, INC. of its Fourth Street
Shop and Southern Carhouse Properties.

In January, 1959, D. C. Transit System, Inc. (hereinafter referred to as the "Company") received \$3,320,000 from the D. C. Redevelopment Land Agency (hereinafter referred to as "R. L. A.") in payment for its Fourth Street Shops and Southern Carhouse, together with certain equipment and an allowance for "consequential damages" incidental to moving and relocation.

The accounting entries originally recorded on the books by the Company, reflecting the treatment accorded the receipts of the sale, are summarized as follows:

Net proceeds from the Sale:

Total purchase price	\$3,320,000.00
Less: Expenses of sale such as recording fees and revenue stamps	<u>3,756.55</u>
	<u>\$3,316,243.45</u>

Accounting for net proceeds:

Estimated undepreciated original cost of buildings and equipment credited to Depreciation Reserve:	
Original cost	\$1,297,018.77
Accrued depreciation to December 31, 1958	<u>745,227.57</u>
	551,791.20

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Provision for future cost of re- locating and removing equipment credited to Suspense Account	325,000.00
Income taxes related to above item credited to accrued taxes	<u>169,000.00</u>
Subtotal	<u>1,045,791.20</u>
Balance of net proceeds	2,270,452.25
Less: Original cost of land credited to Fixed Capital Account for land	<u>89,089.17</u>
Balance of net proceeds treated as profit from sale and credited to Earned Surplus	<u>\$2,181,363.08</u>

The staff of the Commission required more detailed information regarding the breakdown as between land, depreciable property, or other values considered in arriving at the sale price of \$3,320,000 to enable it to pass upon the propriety of the proposed accounting. At the request of the Commission, the Company subsequently furnished the following breakdown used in determining the sale price.

	<u>Appraisal</u>	<u>Reduced by</u>	<u>Compromise Figure</u>
Land	\$1,040,965	\$ - - -	\$1,040,965
Real property improvements	2,071,240	150,000	1,921,240
Consequential damage	640,000	315,000	325,000
Machinery & equipment	176,670	140,000	36,670
Total	<u>\$3,928,875</u>	<u>\$605,000</u>	<u>\$3,323,875</u>
Rounded off	\$3,925,000	\$605,000	\$3,320,000

Based upon this, and other information obtained from the Company and R. L. A., the staff tentatively proposed that the net proceeds from the sale of the property be accounted for as outlined in a letter to the Company under date of April 7, 1959. The staff's initial proposal, insofar as here pertinent, recommended that the distribution of the net proceeds from the sale of the property, after applying the entire reduction of \$3,875 resulting from the rounding process (shown above) against the proceeds from

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the depreciable property, and distributing the expenses of the sale in the amount of \$3,756.55 on a pro rata basis between the proceeds from land and depreciable property, should be as follows:

Land	\$1,039,657.72
Real property improvements	1,915,034.81
Machinery & equipment	36,550.92
Consequential damages	325,000.00
	<u>\$3,316,243.45</u>

Based on the foregoing summary of net proceeds, the accounting initially recommended by the staff of the Commission is summarized as follows:

Land

Net proceeds from sale of land	\$1,039,657.72
Less: Original cost of land	<u>89,089.17</u>
Net profit to be credited to earned surplus	<u>\$ 950,568.55</u>

Depreciable Property

Net proceeds from sale of depreciable property to be credited as salvage to the depreciation reserve	\$1,951,585.73
Original cost of depreciable property to be charged to the depreciation reserve	\$1,297,018.77

Consequential Damages

The Commission's staff is in agreement with the accounting proposed by the Company whereby the payment of \$325,000 for "consequential damages" has been credited to an account captioned, "Reserve for Moving and Relocations." Based on information obtained from R. L. A., however, it is clear that the payment of \$325,000 was made, in large measure, to cover anticipated increased operating costs to be incurred by reason of relocating the shops at a new location farther removed from the center of operations, rather than to cover only the cost of moving

machinery and equipment as has been indicated by the Company.

The Company has advised that the payment of \$325,000 will be subject to Federal income taxes in 1959 in the approximate amount of \$169,000, and has made provision for taxes in this amount out of the proceeds from the sale, thereby reducing the recorded profits on the transaction by this amount. In lieu of this accounting for the related income taxes, the staff has proposed that the provision for taxes in the amount of \$169,000 should be charged against the reserve account for moving and relocations as a deduction from the taxable income to which it is related, thereby leaving a net balance of \$156,000 in the account as the estimated future cost, after making allowance for the related reduction in income taxes, of moving equipment and increased operating costs attributable to route relocations. Under this proposal, as costs are incurred in the future, they would be charged against the reserve account, and the related reduction in income taxes would be credited to the reserve account.

The staff proposal was submitted to the company for its consideration and comment under date of April 7, 1959, and after an informal conference with the Commission at which the views of the Company and the Commission staff were reviewed, the Company by letter dated June 23, 1959, disagreed with the staff proposal and requested approval by the Commission of the accounting as originally recorded on the books. Subsequent to that date, by entry recorded on the books as of June 30, 1959, the Company modified its original proposal in the following respects. Whereas the original entry had given effect to the sale of all shop and substation equipment at the location in question, the modification proposed by the Company was on the basis that no portion of the shop and substation equipment had been included in the sale. The effect of

this modification of the original entry was to restore to fixed capital the original cost of the shop and substation equipment initially retired, with the resulting increase in the profits on the transaction credited to earned surplus of \$87,628.42, summarized as follows:

	<u>Shop Equipment</u>	<u>Substation Equipment</u>	<u>Total</u>
Original cost of property retired	\$192,855.61	\$26,339.10	\$219,194.71
Accrued depreciation at December 31, 1958	<u>115,962.29</u>	<u>15,604.00</u>	<u>131,566.29</u>
Portion of purchase price credited to depreciation reserve as unrecovered cost	<u>\$ 76,893.32</u>	<u>\$10,735.10</u>	<u>\$ 87,628.42</u>

Giving effect to the Company's modification of the accounting for the foregoing items, the profits on the transaction as recorded on the books of the Company were increased from \$2,181,363.08, as heretofore summarized, to \$2,268,991.50.

The staff of the Commission has given consideration to this proposed modification, and based on information obtained from R. L. A., is in agreement that the original entry was in error to the extent that it provided for retirement and sale of the shop and substation equipment in its entirety. The information obtained by the staff is to the effect that the major portion of such equipment is removable and was considered as personal property not included in the sale. However, the breakdown of the selling price of \$3,320,000 furnished by the Company and heretofore summarized, which is supported by information obtained by the Commission's staff from R. L. A., shows that the purchase price did include an amount of \$36,670 for machinery and equipment, adjusted to \$36,550.92 after proration of selling costs.

The staff has been unable to determine just what items of machinery and equipment were included in the sale.

The Company has indicated that it is entirely probable that when the actual abandonment of the property takes place, there will be certain items of equipment and machinery that cannot be moved, as well as certain installation costs with respect to removable equipment that should be retired. The staff has proposed that in the absence of definite information to properly account for the machinery and equipment included in the sale, the portion of the adjusted purchase price related thereto in the amount of \$36,550.92 should be transferred to a suspense account pending determination of the property to be abandoned in connection with moving to a new location, at which time determination will be made as to what portion thereof should be credited to the depreciation reserve and what portion, if any, should be credited to earned surplus.

Giving effect to the reversal of the initial retirement for shop and substation equipment, and to the staff proposal to credit a suspense account with that portion of the purchase price related thereto, the initial proposal by the staff would be modified as follows:

Net proceeds from sale of depreciable property to be credited as salvage to the depreciation reserve (\$1,951,585.73—\$36,550.92)	\$1,915,034.81
Original cost of depreciable property to be charged to the depreciation reserve (\$1,297,018.77—\$219,194.71)	\$1,077,824.06

The staff proposal to credit a suspense account with \$36,550.92 of the net proceeds from the sale pending final determination of the actual retirements to be made for machinery and equipment that is not included in the sale, offers what appears to be a reasonable solution to a problem that cannot be determined on a precise basis at this time. We will, accordingly, give effect to this proposal in our discussions and conclusions set forth hereafter.

Statement of Question Involved

Before dealing with the contentions of the Company and the staff, the Commission deems it essential to pinpoint the principal issue. In so doing, we can dispose of one item not in controversy. The staff and the Company are in agreement that under public utility accounting, the difference between the original cost of land and the selling price is recognized as profit. The net profit of \$950,568.55 on the sale of the land (net proceeds of \$1,039,657.72 less original cost of \$89,089.17) is therefore a proper credit to earned surplus.

Passing, for the moment, the treatment of "consequential damages," it can be seen that the major point of departure between the staff and the Company is the accounting for the proceeds from the sale of depreciable property. Briefly stated, the staff's initial position is that strict compliance with the Uniform System of Accounts, applicable to accounting procedures of utilities under the jurisdiction of this Commission, requires that all amounts received from the sale of depreciable property be credited to the depreciation reserve as salvage. The Company on the other hand, while not disputing the retirement procedures required under the Uniform System of Accounts, takes the position that the sale of depreciable property at an amount considerably in excess of original cost is such an unusual transaction that departure from the normal procedure provided for in the Uniform System of Accounts is justified.

The staff recognizes the unusual nature of the subject transaction and concedes that the Commission might well be justified in authorizing a departure from the accounting procedure normally used in retirement transactions under the Uniform System of Accounts. The staff further takes the position, however, that, if such departure be made, a proper balancing of customer and investor

interest requires different treatment than that adopted by the Company in recording the transaction.

As thus broadly presented, the problem before the Commission is reduced in the first instance to the question of whether or not the unusual transaction under consideration is of such a nature as to justify a departure from the Uniform System of Accounts and, if such departure be justified, to determine the extent thereof.

Discussion and Conclusions

In its consideration of the accounting treatment necessary to properly record the proceeds of the sale by the Company of its Fourth Street Shops and Southern Carhouse to R. L. A., the Commission has had the benefit of the thinking of the Company and of its own staff through correspondence, meetings, and reports. While fully cognizant of the desirability of adhering to the Uniform System of Accounts under normal conditions, we have never recognized the Uniform System of Accounts as an inflexible code from which departures in special or unusual circumstances would not be permitted when authorized by the Commission. Starting from the conceded premise that a strict application of the Uniform System of Accounts requires that the portion of the sale price, representing proceeds from the sale of depreciable property, be credited to the depreciation reserve as salvage, we must evaluate the transaction in light of the circumstances to determine what, if any departure is justified.

The Company has pointed out that the properties retired were sold under threat of eventual condemnation proceedings. It contends, and the staff does not disagree, that receiving approximately \$837,000 more than the original cost from the sale of the depreciable property is such an abnormal occurrence that special accounting treatment is justified. We believe that the fact that application of normal accounting procedures would build the reserve for

depreciation to a point where it would contain approximately 80 per cent more than is necessary to retire 100 per cent of the original cost of these properties justifies a departure from the Uniform System of Accounts. We so find and conclude.

With respect to the extent of departure, the modified entries made on the books of the Company are based on the theory that the depreciation reserve already reflects accrued depreciation to December 31, 1958, in the amount of \$613,661.28¹ on the properties sold. While it is true that the investment in this property, together with all other depreciable property of the Company, has been subject to depreciation accruals in the past, no provision has ever been made for segregating the depreciation reserve by particular units or classes of property. In fact, it has been only since July 1, 1953, that individual accrual rates have been applied for the various classes of property. The staff, in light of these circumstances and other factors discussed below, has submitted an alternate proposal in the event the Commission authorizes a departure from the Uniform System of Accounts. Under this proposal an amount of \$613,661.28 would be credited to the depreciation reserve, in addition to the \$464,162.78² credited to the reserve under the accounting proposed by the Company. The total amount thus credited to the reserve

¹ Accrued depreciation to December 31, 1958	
on total depreciable property	\$745,227.57
Less accrued depreciation on shop and	
substation equipment	<u>131,566.29</u>
Accrued depreciation to December 31, 1958,	
as modified	<u>\$613,661.28</u>
 ² Undepreciated original cost at December 31,	
1958 on total depreciable property	\$551,791.20
Less undepreciated original cost of shop and	
substation equipment	<u>87,628.42</u>
Amount credited to depreciation reserve	
under modified Company proposal	<u>\$464,162.78</u>

would be \$1,077,824.06, or an amount equal to the original cost of the depreciable property sold, exclusive of machinery and equipment. The difference between this amount and the selling price of \$1,915,034.81, or \$837,210.75, would remain as a credit to earned surplus, in addition to the profit of \$950,568.55 on the sale of the land. This approach takes into consideration the right of the Company to recover from its customers through depreciation the loss of service value over the life of the property as measured by the original cost of the property less net salvage realized upon retirement. Since the net salvage recovered upon retirement in this instance exceeded the original cost of the property, it is now established there was no actual retirement loss over its life.

The Company has indicated its intention of claiming exemption from Federal income taxes on the profits from the sale of its Southwest property under the involuntary conversion provisions of the Internal Revenue Code of 1954. As an incident thereto, the proceeds from the sale of the property must be invested in replacement property by the end of 1960. The Code further provides that to the extent that such replacement property is constructed from nontaxable gain under the involuntary conversion provision, said property is not subject to future depreciation for tax purposes.

In further support of the reasonableness of the proposed alternate accounting treatment, the staff points out that under the Company proposal, the exemption from taxes would be for the exclusive benefit of the investors, whereas the customers would be burdened in the future by higher taxes as a result of the loss of the normal depreciation deduction for tax purposes. In our opinion, this result under the Company proposal warrants careful consideration of the equities involved.

In light of the franchise of the Company requiring a gradual program of conversion from railway to bus opera-

tions over a seven-year period from July 24, 1956, we are unable to disassociate the instant transaction from the imminent retirement of all rail property under the mandate contained in the franchise. We cannot ignore the probability that full provision for depreciation will not have been provided when the rail facilities are abandoned and retired by reason of conversion. The Company has consistently taken the position that any retirement loss in this connection should be recovered by charges against the customers, and the staff has heretofore indicated its agreement. However, if the customers are to be required to bear the burden of extraordinary retirement losses incident to the whole conversion program, it appears equitable that they should share, at least to some extent, in extraordinary retirement gains of the nature here under consideration.

The Company takes the position that future losses on disposal of railway property may or may not occur and that known credits should not be used to offset future unknown charges. The Commission agrees that extraordinary retirement losses resulting from the abandonment of railway property prior to the completion of its normal service life cannot be accurately determined at this time. However, we regard extraordinary retirement losses as belonging in the same category as track removal and repaving costs for which provision is presently being made as a charge against the ratepayers on an estimated basis over a ten-year period without objection by the Company. In view of the virtual certainty of future extraordinary retirement losses in connection with conversion, we give little weight to this contention by the Company.

Since accounting is not an exact science, our judgment must of necessity be based upon factors not subject to precise measurement. Our investigation and study of the matter has led to the conclusion that the alternate pro-

posal of the staff with respect to the accounting treatment to be accorded the proceeds from the sale of the depreciable property provides an equitable solution to a difficult problem, maintaining, as far as possible, what seems to be a fair balance between the interests of the public and those of the Company's investors. We so find and conclude.

With respect to the accounting treatment to be accorded the accrual for Federal income taxes in the amount of \$169,000 related to the payment of \$325,000 for consequential damages, we recognize that while the staff proposal will have the immediate effect of increasing the amount credited to earned surplus as profits by the former amount, there will be no difference in the ultimate result under either plan.

The Company's method in effect treats the tax of \$169,000 as a direct charge to earned surplus, with no effect on reported income for the year. When the estimated costs of \$325,000 are incurred, presumably they will be charged against the reserve and the related tax credit of \$169,000 will flow through income with a corresponding increase in earned surplus. Thus, the initial charge against earned surplus is balanced by the future credit. Under the staff plan, the tax of \$169,000 is directly associated with the \$325,000 at all times. The reserve is charged with the tax expense at this time, to be offset later with the tax credit when the costs of moving and relocating are actually incurred. Under this method, net income, as well as earned surplus, is unaffected either now or later.

We agree with the staff proposal that the income tax accruals should be associated with the revenues and expenses to which they are related, and that the provision for the estimated future cost of moving equipment and increased operating costs attributable to route relocations should be on a "net of taxes" basis as heretofore outlined, with the proviso that any balance remaining in the

reserve account for moving and relocations, after all proper charges thereto have been recorded, shall be disposed of as directed by the Commission. We so find and conclude. Accordingly,

IT IS ORDERED:

That D. C. Transit System, Inc. shall make the necessary adjustments in its accounts to give effect to the accounting treatment of the proceeds from the sale of its Fourth Street Shops and Southern Carhouse Properties as set forth in the appendix attached hereto.

A TRUE COPY:

By the Commission:

Norman B. Belt
Executive Secretary

Chief Clerk

Appendix to Order No. 4577

D. C. TRANSIT SYSTEM, INC.

Proposed entries to correct accounting for
proceeds from sale of Fourth Street Shop
and Southern Carhouse Properties

1. Earned Surplus (Account 451-306)	\$613,661.28	
Accrued depreciation (Account 443-604)		\$584,470.88
Accrued depreciation (Account 443-608)		4,703.52
Accrued depreciation (Account 443-610)		24,486.88

To transfer from Earned Surplus to
Accrued depreciation the amounts estimated
to represent accrued depreciation
on the buildings and track at the
Fourth Street Shops and Carhouse in
conformance with the accounting prescribed
by the Public Utilities Commission.

2. Reserve for Moving and Relocations— (Account 446R)	\$169,000.00	
Earned Surplus (Account 451-306)		\$169,000.00

To restore to Earned Surplus the tax
charged thereto applicable to amount
received for the estimated cost of
moving and relocations.

3. Earned Surplus (Account 451-306)	\$ 36,550.92	
Reserve for Salvage on machinery and equipment—Southwest Property— (Account 446S)		\$ 36,550.92

To reserve that portion of the proceeds
from the sale of the Fourth Street Shop
and Southern Carhouse Properties representing
the payment by R. L. A. for machinery and
equipment pending determination of the
equipment to be abandoned and retired.

EXHIBIT B, ANNEXED TO PETITION

Petition for Reconsideration

BEFORE THE
PUBLIC UTILITIES COMMISSION
OF THE DISTRICT OF COLUMBIA

P.U.C. No. 3574/16

FORMAL CASE NO.

In the Matter of Accounting for Proceeds from
Sale by D. C. Transit System, Inc. of its Fourth
Street Shops and Southern Carhouse Properties.

PETITION FOR RECONSIDERATION

Comes now petitioner, D. C. Transit System, Inc. (hereinafter referred to as "D. C. Transit") pursuant to Public Law 757, 84th Congress, 2nd Session, 70 Stat. 598 and pursuant to the Act of March 4, 1913, 37 Stat. 974, as amended (D. C. Code, Title 43, Section 704), and respectfully petitions the Public Utilities Commission of the District of Columbia (hereinafter referred to as the "Commission") to reconsider its Order No. 4577 dated September 30, 1959 and as grounds for such reconsideration, D. C. Transit respectfully alleges the following errors in such Order:

(1) The Commission erred in its statement that the Company contends that receiving approximately \$837,000 more than original cost from the sale of the depreciable property is such an abnormal occurrence that special accounting treatment is justified.

(2) The Commission erred in finding and concluding that since the net salvage recovered upon the sale of the property exceeded the original cost thereof, it is now established there was no actual retirement loss over its life.

(3) The Commission erred in relating the sale of the Southwest properties to the imminent retirement of all rail property under the conversion mandate of Section 7 of the Company's franchise.

(4) The Commission erred in finding and concluding that the alternate accounting proposal of the staff with respect to the accounting treatment to be accorded the proceeds from the sale of the depreciable property provides an equitable solution and maintains a fair balance between the interests of the public and those of the Company's investors.

(5) The Commission erred in ordering the Company to make the Adjustment Entry Number 1 described in the Appendix attached to the Order herein.

WHEREFORE, D. C. Transit respectfully prays that:

A. The Commission reconsider its Order No. 4577 dated September 30, 1959 and that it modify such Order in accordance with this Petition;

B. The Commission grant such other and further relief as may be just and proper.

Dated this 29th day of October, 1959.

Respectfully submitted,

D. C. TRANSIT SYSTEM, INC.
3600 M Street, N. W.
Washington, D. C.

By: /s/ O Roy Chalk
O. Roy Chalk
President

/s/ Harvey M. Spear
Harvey M. Spear

Attorney for D. C. Transit System, Inc.
3600 M Street, N. W.
Washington 7, D. C.

DISTRICT OF)
COLUMBIA) SS:

O. ROY CHALK, being first duly sworn on his oath, deposes and says, that he is the President of D. C. Transit System, Inc., that he has read the foregoing petition by him subscribed, that he knows the contents thereof, and that he is informed and believes that the matters and things therein stated are true.

/s/ O. Roy Chalk
O. Roy Chalk

Subscribed and sworn to before me this 29th day of October, 1959.

/s/ Dean R. Long
Notary Public
My Commission Expires
September 14, 1961

MOTION

(Filed June 24, 1960)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 3306-59

D. C. TRANSIT SYSTEM, INC., PETITIONER

v.

PUBLIC UTILITIES COMMISSION OF THE
DISTRICT OF COLUMBIA, RESPONDENT

MOTION OF THE PUBLIC UTILITIES COMMISSION
TO DISMISS APPEAL OR FOR SUMMARY
JUDGMENT

Respondent Public Utilities Commission, by its attorneys, moves the Court to dismiss the petition of appeal filed in this action on the grounds that it fails to state a claim upon which relief can be granted in that:

- (a) The petitioner's prayer raises issues not raised or considered in the petition for reconsideration filed with the Commission, which is prerequisite to the right of review of orders and decisions of the Commission.
- (b) The petitioner, without citation of authority or any basis in the record, other than counsel's power of statement, prays the Court to vacate and set aside an order dealing with public utility accounting, a subject matter expressly placed under the exclusive jurisdiction and control of the Commission by the Congress of the United States.

In the alternative, Respondent Commission moves the Court to enter summary judgment in its favor on the

ground that the petition of appeal, when considered together with the certified record filed in this case, shows there is no genuine issue as to any material fact and that the Respondent Commission is entitled to judgment as a matter of law.

/s/ Chester H. Gray
CHESTER H. GRAY
General Counsel

/s/ Lloyd B. Harrison
LLOYD B. HARRISON
Counsel

/s/ George F. Donnell
GEORGE F. DONNELLA
Counsel

Attorneys for Respondent,
Public Utilities Commission,
District Building
Washington 4, D. C.

Certificate of Service

A copy of Motion of the Public Utilities Commission to Dismiss Appeal or for Summary Judgment together with Points and Authorities, in support thereof, was mailed, postage prepaid, to Harvey M. Spear, Attorney for Petitioner, 3600 M St., N.W., Washington, D. C., this 11th day of December, 1959.

/s/ George F. Donnell
GEORGE F. DONNELLA
Counsel

CROSS-MOTION

(Filed March 31, 1960)

• • • •

PETITIONER'S CROSS-MOTION FOR
SUMMARY JUDGMENT

Petitioner moves the Court, pursuant to Rule 56 of the Federal Rules of Civil Procedure, for an order granting a summary judgment in favor of the petitioner and against the respondent upon the ground that there is no genuine issue of any material fact and that petitioner is entitled to a judgment as a matter of law.

Dated: Washington, D. C.
March 31, 1960

/s/ Harvey M. Spear
HARVEY M. SPEAR
Attorney for Petitioner
3600 M Street, N. W.
Washington 7, D. C.

Certificate of Service

A copy of the attached Petitioner's Cross-Motion for Summary Judgment, together with the Points and Authorities in Opposition to Respondent's Motion to Dismiss the Appeal or for Summary Judgment and in Support of Petitioner's Cross-Motion for Summary Judgment, was mailed, postage prepaid, this 31st day of March, 1960, to Chester H. Gray, Esq., Corporation Counsel, District of Columbia, Attorney for Respondent, District Building, Washington 4, D. C.

/s/ Harvey M. Spear
HARVEY M. SPEAR

MEMORANDUM

(Filed June 10, 1960)

• • • •

MEMORANDUM

The Court is of the opinion that Order No. 4577 of the respondent, Public Utilities Commission, dated September 30, 1959 is not unreasonable, arbitrary or capricious. Accordingly, the motion of the respondent for summary judgment will be granted and the cross-motion of the petitioner for summary judgment will be denied.

/s/ Joseph C. McGarraghy
JUDGE

June 10, 1960

ORDER

(Filed June 24, 1960)

• • • •

ORDER

Upon consideration of the Petitioner's appeal from the Public Utilities Commission Order No. 4577; the certified record of the proceedings had before the Commission; the motion of the respondent Commission to dismiss the appeal or in the alternative for summary judgment and the Petitioner's cross-motion for summary judgment; the points and authorities submitted in support of or in opposition to the said motions; and after oral argument by the parties on June 2, 1960; and it appearing to the Court that the order appealed from is not unreasonable, arbitrary or capricious, and it further appearing that the appeal raises no genuine issue as to any material fact and that Order No. 4577 was promulgated by the Commission

pursuant to statutory authority, it is, by the Court, this 24th day of June, 1960,

ORDERED AND ADJUDGED: That the motion of respondent Public Utilities Commission for summary judgment is hereby granted; that the petition of appeal is hereby dismissed; and that Order No. 4577 of the Public Utilities Commission of the District of Columbia dated September 30, 1959, be, and it is hereby, affirmed; and

BE IT FURTHER ORDERED AND ADJUDGED: That the cross-motion of petitioner, D. C. Transit System, Inc., for summary judgment, be, and it is hereby, denied.

/s/ J. McGarraghy
JUDGE

NOTICE OF APPEAL

(Filed July 22, 1960)

* * * *

Notice is hereby given that D. C. Transit System, Inc., petitioner above named, hereby appeals to the United States Court of Appeals for the District of Columbia from the order of the United States District Court for the District of Columbia (Hon. Joseph C. McGarraghy) entered on June 24, 1960 granting the motion of respondent Public Utilities Commission of the District of Columbia for summary judgment, dismissing the petition of appeal herein, affirming Order No. 4577 of the Public Utilities Commission of the District of Columbia dated September 30, 1959, and denying the cross-motion of petitioner, D. C. Transit System, Inc., for summary judgment.

/s/ Harvey M. Spear
HARVEY M. SPEAR
Attorney for Petitioner
D. C. Transit System, Inc.
3600 M Street, N. W.
Washington, D. C.

Dated:
July 22, 1960

CERTIFICATION OF RECORD ON APPEAL

(Filed December 11, 1959)

PUBLIC UTILITIES COMMISSION
OF THE DISTRICT OF COLUMBIA

P.U.C. No. 3574/16

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Civil Action No. 3306-59

D. C. TRANSIT SYSTEM, INC., PETITIONER

VS.

PUBLIC UTILITIES COMMISSION OF THE
DISTRICT OF COLUMBIA, RESPONDENT

CERTIFICATION OF RECORD ON APPEAL

There is transmitted herewith the documents listed below, constituting the record in P.U.C. No. 3574/16, before the Public Utilities Commission of the District of Columbia, "In the matter of Accounting for the Proceeds from Sale by D. C. Transit System, Inc. of its Fourth Street Shop and Southern Carhouse Properties". The said record is transmitted in accordance with the provisions of Paragraph 65 of the Act of March 4, 1913 (Sec. 43-705, D.C. Code), creating the Public Utilities Commission, as amended by the Act of August 27, 1935.

The record consists of the following:

1. A letter dated March 18, 1959, from the Commission to James H. Flanagan.
2. A letter dated March 20, 1959, from James H. Flanagan to the Commission.
3. A letter dated April 7, 1959, from the Commission to James H. Flanagan.

4. A letter dated June 23, 1959, from James H. Flanagan to the Commission.
5. Order No. 4577 dated September 30, 1959, containing Discussion and Conclusion and ordering accounting adjustments to be made as specified.
6. Petitioner's application for reconsideration of Order No. 4577 dated October 30, 1959.
7. Order No. 4587, denying petitioner's application for reconsideration, dated November 2, 1959.

By direction of the Commission:

/s/ Norman B. Belt
NORMAN B. BELT
Executive Secretary.

I, Norman B. Belt, Executive Secretary of the Public Utilities Commission, hereby certify that the documents and papers designated hereinabove constitute the record of investigation before the Commission in the above-stated cause upon which the Commission's Order No. 4577 was based.

In testimony thereof, I hereunto subscribe my name and affix the seal of the Public Utilities Commission this 10th day of December, 1959.

/s/ Norman B. Belt
NORMAN B. BELT
Executive Secretary

LETTER OF MARCH 18, 1959

PUBLIC UTILITIES COMMISSION
OF THE DISTRICT OF COLUMBIA

Washington 4, D. C.

MAR 18, 1959

Mr. James H. Flanagan, Vice President
and Comptroller
D. C. Transit System, Inc.
36th and M Streets, Northwest
Washington, D. C.

Dear Mr. Flanagan:

The staff of the Commission has called our attention to the fact that in January of 1959 the books of the Company reflect the accounting for the sale of your Southwest property to the D. C. Redevelopment Land Agency, including a credit to Earned Surplus in the amount of \$2,181,363.08 as profit on the sale.

To enable the staff to verify the propriety of the accounting as recorded on the books, you are requested to furnish the Commission with a copy of any data you may have in your files showing the basis for arriving at the total purchase price of \$3,320,000, with particular reference to the portion thereof that might be specifically applicable to land, buildings, equipment or other elements of value.

Your prompt cooperation in this matter will be appreciated.

Very truly yours,

/s/ George E. C. Hayes
GEORGE E. C. HAYES
Chairman

LETTER OF MARCH 20, 1959

D. C. TRANSIT SYSTEM, INC.
 Thirty-Sixth and M Street, N.W.
 Washington, D. C.

March 20, 1959

Honorable George E. C. Hayes, Chairman
 Public Utilities Commission
 of the District of Columbia
 District Building
 Washington 4, D. C.

Dear Mr. Chairman:

Replying to your letter of March 18, 1959, the total purchase price of \$3,320,000 paid by the D. C. Redevelopment Land Agency for certain property of D. C. Transit System, Inc. located in Southwest Washington was arrived at as follows:

	<u>Appraisal</u>	<u>Reduced by</u>	<u>Compromise Figure</u>
Land	\$1,040,965	—	\$1,040,965
Real Property	2,071,240	\$150,000	1,921,240
Consequential Damages	640,000	315,000	325,000
Machinery and Equipment	176,670	140,000	36,670
Total	\$3,928,875	\$605,000	\$3,323,875
Rounded off	\$3,925,000	\$605,000	\$3,320,000

The foregoing basis was determined at a conference held between officials of D. C. Redevelopment Land Agency and of D. C. Transit System, Inc.

Very truly yours,

/s/ J. H. Flanagan

J. H. FLANAGAN

Vice President and Comptroller

LETTER OF APRIL 7, 1959

PUBLIC UTILITIES COMMISSION
OF THE DISTRICT OF COLUMBIA

Washington 4, D. C.

Apr 7, 1959

Mr. James H. Flanagan, Vice President
and Comptroller
D. C. Transit System, Inc.
36th and M Streets, Northwest
Washington, D. C.

Dear Mr. Flanagan:

Your letter of March 20, 1959, showing the basis for arriving at the purchase price of \$3,320,000 paid by the D. C. Redevelopment Land Agency for your "Fourth Street Shops and Southern Carhouse Property", was referred to the staff of the Commission for consideration. Based upon the information set forth in your letter, together with other available information, the staff has questioned the accounting recorded on the books for the proceeds from the sale of this property.

As reported by the staff of the Commission, the Uniform System of Accounts under which D. C. Transit System, Inc. operates provides for crediting earned surplus with any profit realized on the sale of land. With respect to the sale of depreciable property, however, the Uniform System of Accounts provides that any amount received from the sale thereof represents the salvage value of the property and as such should be credited to the depreciation reserve.

Under the facts in the instant case, crediting the depreciation reserve with the proceeds from the sale of the depreciable property will result in a credit balance in the reserve somewhat in excess of the amount required to

meet the retirement of the original cost of the property. The staff recognizes that this is not the normal situation to be expected in the retirement of depreciable property, but expresses the view that the accounting, which will be proposed hereafter, is justified when consideration is given to the fact that it is anticipated that the Company will incur extraordinary property losses not provided for in the depreciation reserve in connection with the retirement of rail property incident to conversion. The Company has already indicated that such property losses should be made up by charges against the customers, and the staff has previously indicated its acquiescence in this view when the amount of any such property loss can be determined. In the opinion of the staff, equitable treatment of both the customers and the investors requires that the extraordinary salvage value realized on the sale of the Southwest property be credited to the depreciation reserve where it will be available to partially offset the anticipated extraordinary property losses to be incurred in connection with conversion.

Based on a staff study, the distribution of the net proceeds from the sale of the property, after applying the reduction of \$3,875 in the rounding process in its entirety against the proceeds from the depreciable property, and distributing the expenses of the sale in the amount of \$3,756.55 on a percentage basis between the proceeds from land and depreciable property, would be as follows:

Land	\$1,039,657.72
Depreciable Property	1,951,585.73
Consequential Damages	<u>325,000.00</u>
Net Proceeds	<u>\$3,316,243.45</u>

Any additional expenses incident to the sale of the property that cannot be associated directly with either land or depreciable property should be distributed in a like manner on a percentage basis between the two items.

Based on the foregoing summary of net proceeds, the accounting recommended by the staff of the Commission is summarized as follows:

Land

Net proceeds from sale of land	\$1,039,657.72
Less: Original cost of land	<u>89,089.17</u>
Net profit to be credited to earned surplus	<u>\$ 950,568.55</u>

Depreciable Property

Net proceeds from sale of depreciable property to be credited as salvage to the depreciation reserve	\$1,951,585.73
Original cost of depreciable property to be charged to the depreciation reserve	\$1,297,018.77

Consequential Damages

Available information shows that the item of \$325,000 labeled "Consequential Damages", represents a partial allowance by R.L.A. of a total amount of \$640,000 claimed by the Company as compensation for estimated increased operating costs to be incurred over the remaining life of the streetcar system by reason of conducting the Southwest operations from other locations. The Company's claim was based on an estimate of such additional costs included in an appraisal by Stone & Webster for the Company in the latter part of 1958. In this appraisal, the \$640,000 was spread in reducing amounts over a ten-year period, indicated as the estimated remaining economic life of the streetcar system. It is the understanding of the staff that these facts were considered by R.L.A. in arriving at the agreed payment of \$325,000. It is possible that other anticipated costs, such as the cost of relocating materials and supplies, may also have been considered in the final settlement of \$325,000.

It is the opinion of the staff that the allowance of \$325,000 represents an advance payment for expenses to

be incurred in the future, and as such should be recorded on the books as a deferred credit available for meeting such expenses as they are incurred. The staff has been advised that in the opinion of the Company accountants this payment of \$325,000 will be subject to Federal income taxes in 1959 in the approximate amount of \$169,000, the balance of the net proceeds from the sale being exempted from income taxes under the involuntary conversion provisions of Section 1033 of the Internal Revenue Code of 1954.

Provision has been made on the books for the income tax liability by deducting from the net proceeds of the sale the estimated liability of \$169,000, thereby resulting in a reduction in the reported profit on the whole transaction in a like amount. It is the staff's opinion that provision for income taxes should have been made by charging the deferred credit account, thereby leaving a net balance in the deferred credit account of \$156,000. Disposition of this net balance of \$156,000 in the deferred credit account should be made as the expenses are incurred, either by releasing the amount as a credit to operating income and exempting same from taxable income in the calculation of Federal income taxes, or by charging the expenses against the deferred credit account, and crediting same with the related reduction in income taxes.

Before arriving at any conclusion on the staff recommendations set forth above, the Commission would like to have the benefit of any comments you may care to make. If desired, the staff will be available for discussing this matter further in an informal conference at either the staff or the Commission level.

Very truly yours,

/s/ George E. C. Hayes
GEORGE E. C. HAYES
Chairman

LETTER OF JUNE 23, 1959

D. C. TRANSIT SYSTEM, INC.
Thirty-Sixth and M Street, N.W.

Washington, D. C.

June 23, 1959

Hon. George E. C. Hayes, Chairman
Public Utilities Commission
Washington, D. C.

Dear Mr. Chairman:

With reference to your letter of April 7, 1959 relating to the accounting treatment given the retirement of the "Fourth Street Shops and Southern Carhouse property" and to a recent meeting on June 9, 1959 with the Commission, we should like to state the views that led to the recording of the accounting entries in their present form.

In your letter you indicated that "the staff recognized that this is not the normal situation to be expected in the retirement of property". We also felt that it was not a "normal situation" and chose therefore to depart from the usual retirement accounting procedures whereby all proceeds from sale of a depreciable property are credited to the depreciation reserve. Mr. Falk indicated in the June 9 meeting that the staff had no quarrel with the amount of proceeds allocated to the reserve for depreciation since the Company had used an earlier study by the Commission's consultant, Mr. Ingoldsby, as the basis for determining the undepreciated cost of the remaining assets.

It therefore appears from your letter of April 7, 1959 that the only reason for withholding approval of this accounting lies with the Commission staff's interest in retaining a portion of the proceeds in a reserve to absorb future losses on disposal of railway property, which losses may or may not occur.

We feel that this approach is completely erroneous and represents nothing more than an illogical offsetting of known credits against unknown charges. It would distort the accounting by combining dissimilar transactions into one confusing entanglement.

The effect of placing all the allocated net proceeds from the sale of depreciable property into the depreciation reserve would be to set aside approximately \$650,000 more than the original cost of these properties. We find no logic in the suggestion that we build this reserve to a point where it would contain 50.47% more reserve than is necessary to retire 100% of the original cost of these properties.

We submit that the consideration received from the sale of the land and buildings was the fair value of these properties, arrived at through arms-length negotiations. The so-called increment of the proceeds received over the original cost of the depreciable properties did not represent appreciation of the buildings. Rather, it represented depreciation or decline in value of the dollar. Substantially 30% of the Fourth Street Shop was built prior to 1915. The balance was constructed since then with the last significant additions, totaling \$191,000, being constructed in 1949. The construction cost index published by U. S. Department of Labor and U. S. Department of Commerce lists (on page 55 of the 1958 edition) building construction costs indexes as follows:

1915	34
1949	105
1956	154

The situation with Southern Carhouse is substantially the same. Approximately half of this property was constructed prior to 1915.

The point of this discussion is simply this: We sold our land and buildings. We were paid for our land and

buildings and certain other damages. We were not paid the sum of \$3,320,000 on the premise that we might lose money on another type of property at a future date.

The properties that were retired were sold under the threat of condemnation proceedings. If the Company had protested the award of the D. C. Redevelopment Land Agency, the settlement could have been delayed for an indefinite period of time, perhaps even as long as 1963 or 1964. But the facts are that management of this Company felt that the award was fair and decided to consummate the sale. Therefore, it is our opinion that this case ought to be decided on its own merits without reference to any other contingencies.

The last part of your letter of April 7 discusses the "net of taxes" approach to the recording of the reserve for future relocation and removal costs. This approach is basically wrong for the reasons which we shall recite.

First of all, this approach is inconsistent with the other reserves which the Company has established; such as, the reserve for injuries and damages and the reserve for track removal and repaving.

Secondly, the Company was paid these damages for a specific purpose. We have reserved for these future costs, and we are not anxious to include in our operating expense accounts, non-recurring costs in future years which would only serve to confuse the comparability of our statements. This would be the case if we were to follow the staff's suggestions. To state it simply, we regard the moving costs for which we were paid, as a non-operating type of function which ought not to be saddled upon the transit riders. We think our accounting treatment accomplishes this purpose. It is true that taxes may be reduced at some future date as a result of the Company paying moving costs and charging the same to the reserve established therefor. But it is always possible for the Commission

to give the proper credit for such a tax savings to the transit riders at the proper time in any future rate proceedings where the savings would be a factor.

In view of the foregoing, we request that the Commission give its approval to the accounting treatment of the transaction covering the sale in January 1959 of property in Southwest Washington to the D. C. Redevelopment Land Agency.

Very truly yours,

/s/ J. H. Flanagan

J. H. FLANAGAN

Vice President and Comptroller

JHF:ELL

ORDER NO. 4577

DATED SEPTEMBER 30, 1959

CONTAINING DISCUSSION AND CONCLUSION,
AND ORDERING ACCOUNTING ADJUSTMENTS
TO BE MADE AS SPECIFIED

See Exhibit A to Petition of Appeal, page 8a supra.

PETITIONER'S APPLICATION FOR
RECONSIDERATION OF ORDER NO. 4577
DATED OCTOBER 30, 1959

See Exhibit B to Petition of Appeal, page 22a supra.

ORDER NO. 4587

PUBLIC UTILITIES COMMISSION OF THE
DISTRICT OF COLUMBIA

Order No. 4587

November 12, 1959

P.U.C. No. 3574/16

IN THE MATTER OF
Accounting for Proceeds from Sale by D. C.
TRANSIT SYSTEM, INC. of its Fourth Street
Shop and Southern Carhouse Properties.

ORDER DENYING PETITION FOR
RECONSIDERATION

On October 30, 1959, D. C. Transit System, Inc., petitioned this Commission to reconsider its Order No. 4577 entered September 30, 1959, in the above-entitled matter.

Upon consideration of the allegations of error contained in the petition for reconsideration, the Commission finds no matters of substance not previously considered and

passed upon, nor any matter which would warrant findings or conclusions different in any respect from those reflected by Order No. 4577. Therefore, IT IS ORDERED:

That the petition of D. C. Transit System, Inc. for reconsideration of Order No. 4577 be, and it is hereby, denied.

A TRUE COPY:

By the Commission:

Norman B. Belt
Executive Secretary

Chief Clerk

ms

MOTION FOR EXTENSION OF TIME

(Filed October 6, 1960)

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA

Appeal No. 15,967

D. C. TRANSIT SYSTEM, INC., 3600 M Street, N.W.
Washington 7, D. C., APPELLANT

v.

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA,
District Building, Washington 4, D. C., APPELLEE

MOTION FOR EXTENSION OF TIME

D. C. Transit System, Inc., appellant herein, by and through its attorneys, respectfully requests that the time limited for the filing of its brief herein be extended to and including November 1, 1960, and as reasons therefor states:

1. That appellant's brief is presently due to be filed on or before October 10, 1960.

2. That appellant's undersigned counsel has, because of the pressure of matters including the preparation of a rate proceeding before the Public Utilities Commission, D. C. hearings on which commenced September 29, 1960, and other litigation before the United States District Court, D. C. and the Municipal Court, D. C., been unable to devote his full attention to the brief to be filed herein.

3. That the resignation of a member of appellant's legal staff early in the month of September, 1960 resulted in an increased burden on the undersigned counsel, and prevented his devoting the necessary attention to the subject brief.

4. That, as evidenced by the stipulation attached hereto, counsel for the appellee has agreed to the requested extension.

/s/ Owen J. Malone
OWEN J. MALONE
Co-counsel for Appellant

CERTIFICATE OF SERVICE

A copy of the foregoing Motion for Extension of time was mailed, postage prepaid, to George F. Donnella, Esquire, attorney for appellee, District Building, Washington 4, D. C., this 6th day of October, 1960.

/s/ Owen J. Malone
OWEN J. MALONE
3600 M Street, N.W.

STIPULATION

(Filed October 6, 1960)

• • • •

STIPULATION

D. C. Transit System, Inc., appellant, and the Public Utilities Commission of the District of Columbia, appellee, by and through their respective attorneys, pursuant to Rule 18(f) of the rules of this Court, hereby stipulate and agree that the time limited for the filing of appellant's brief herein be extended to and including November 1, 1960.

/s/ Harvey M. Spear
HARVEY M. SPEAR
Attorney for Appellant
3600 M Street, N.W.
Washington 7, D. C.

/s/ George F. Donnell
GEORGE F. DONNELLA
Asst. Corporation Counsel, D. C.
Attorney for Appellee
District Building
Washington 4, D. C.

47 a

ORDER

(Filed October 11, 1960)

• • • •

ORDER

It is ordered that appellant's motion for extension of time to and including November 1, 1960 within which to file its brief is granted pursuant to Rule 31(k)(2) of this court.

FOR THE COURT:

/s/ Joseph W. Stewart
JOSEPH W. STEWART, Clerk

Dated: October 11, 1960

BRIEF FOR APPELLEE PUBLIC UTILITIES COMMISSION

**UNITED STATES COURT OF APPEALS
For The District Of Columbia**

No. 15, 967

D. C. TRANSIT SYSTEM, INC.

Appellant,

v.

PUBLIC UTILITIES COMMISSION

Appellee.

**Appeal From The United States District Court
For The District Of Columbia**

CHESTER H. GRAY
General Counsel

GEORGE F. DONNELLA
Counsel

ANDREW G. CONLYN
Counsel

**Attorneys for Appellee
Public Utilities Commission
District of Columbia
District Building
Washington 4, D. C.**

United States Court of Appeals
For the
District of Columbia Circuit

FILED DEC 22 1960

Joseph W. Stewart
CLERK

BRIEF FOR APPELLEE PUBLIC UTILITIES COMMISSION

**UNITED STATES COURT OF APPEALS
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ANDREW G. CONLYN
Counsel

**Attorneys for Appellee
Public Utilities Commission
District of Columbia
District Building
Washington 4, D. C.**

United States Court of Appeals
For the
District of Columbia Circuit

FILED DEC 22 1968

Joseph W. Stewart
CLERK

QUESTIONS PRESENTED

Where a utility received more for the sale of its depreciable property than its original cost, and the Public Utilities Commission authorized a departure from the Uniform System of Accounts applicable to the sale of such property, the effect of such departure being that the utility was enabled to add \$837,210.75 to its earned surplus account which it would otherwise not be entitled to, the questions presented in the opinion of the appellee, are:

1. Was the Public Utilities Commission correct in determining that there was no loss over the service life of the property?
2. Can D. C. Transit System, Inc. reasonably be heard to complain, because the Commission, in prescribing accounting for the proceeds of the sale of part of the Company's depreciable property, limited the extent of its departure from the Uniform System of Accounts by a consideration of the public interest involved in the transaction?
3. Where the Congress has committed the determination of accounting matters involving utilities to the judgment and discretion of the Commission, can an accounting order of the Commission be invalidated on appeal in the absence of any factual showing by appellant that the order is arbitrary, capricious or unreasonable?

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CASES CITED

<u>Alabama Power Co. v. F. P. C., 75 U.S.App. D. C. 315,</u> <u>128 F. 2d. 280, (Cert. d. 317 U. S. 652).</u>
<u>American Tel. & Tel. Co. v. U. S., 299 U.S. 232, 236, 237,</u> <u>57 S. Ct. 170, 81 L. Ed. 178.</u>

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Arkansas Power & Light Co. v. F. P. C.
87 U.S.App. D.C. 385, 185 F.2d. 751,
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Clarion River Power Co. v. Smith
61 App. D.C. 186, 59 F.2d. 861
(Cert. d. 287 U.S. 639).....

Kansas City So. Ry. v. U. S., 231 U.S. 423-444-456,
34 S.Ct. 125, 58 L. Ed. 296.....

Lindheimer v. Illinois Telephone Co.,
292 U.S. 151-167, 65 S.Ct. 658, 78 L. Ed. 1182.....

Norfolk & Western R.R. Co. v. U. S.
287 U.S. 134-141, 53 S.Ct. 52,
77 L. Ed. 218.....

Northwestern Electric Co. v. F. P. C., 321 U.S. 119,
64 S.Ct. 451, 88 L. Ed. 596.....

STATUTE CITED

Act of March 4, 1913, 37 Stat. 974, Sec. 8:

Par. 11, D. C. Code, Sec. 43-310 (1951 edition).....

Par. 15, D. C. Code, Sec. 43-314 (1951 edition).....

UNITED STATES COURT OF APPEALS
For The District Of Columbia Circuit

No. 15, 967

D. C. TRANSIT SYSTEM, INC.

Appellant,

v.

PUBLIC UTILITIES COMMISSION

Appellee.

Appeal From The United States District Court
For The District Of Columbia

BRIEF FOR APPELLEE PUBLIC UTILITIES COMMISSION

COUNTERSTATEMENT OF THE CASE

The statement of the case made by appellant, D. C. Transit System, Inc. (hereinafter referred to as the Company) contains statements and arguments designed to give the impression that the Public Utilities Commission (hereinafter referred to as the Commission), by its Accounting Order No. 4577 deprived the Company of earned

surplus in the amount of \$613,661.28. Such is not the case. The fact is, that as a result of the Accounting Order complained of, the Company was permitted to retain in earned surplus \$837,210.75 which, in the absence of the departure from the Uniform System of Accounts authorized by Order No. 4577, the Company would not be entitled to under that system of accounts applicable to utilities under the jurisdiction of the Commission.

The Commission, therefore, deems it necessary to make a counterstatement of the case embodying only those undisputed facts necessary to understand the issue it believes to be raised on appeal.

In January, 1959, the Company received \$3,320,000 from the D. C. Redevelopment Land Agency (hereinafter referred to as "R. L. A.") in payment for its Fourth Street Shops and Southern Carhouse, together with certain equipment and an allowance for "consequential damages" incidental to moving and relocation.

The accounting entries originally recorded on the books by the Company, reflecting the treatment accorded the receipts of the sale, and constituting a departure from prescribed accounting without Commission authority, (JA 8a) are summarized as follows:

Net proceeds from the sale:		
Total purchase price		\$3, 320, 000. 00
Less: Expenses of sale such as recording fees and revenue stamps.....		3, 756. 55
		<u>\$3, 316, 243. 45</u>
Accounting for net proceeds:		
Estimated undepreciated original cost of buildings and equipment credited to Depreciation Reserve:		
Original Cost.....	\$1, 297, 018. 77	
Accrued depreciation December 31, 1958.....	<u>745, 227. 57</u>	551, 791. 20
Provision for future cost of relocating and removing equipment credited to Suspense Account.....		325, 000. 00
Income taxes related to above item credited to accrued taxes.....		169, 000. 00
Subtotal.....		<u>1, 045, 791. 20</u>
Balance of net proceeds.....		<u>2, 270, 452. 25</u>
Less: Original cost of land credited to fixed Capital Account for land.....		<u>89, 089. 17</u>
Balance of net proceeds treated as profit from sale and credited to Earned Surplus.....		<u>\$2, 181, 363. 08</u>

The staff of the Commission required more detailed information regarding the breakdown as between land, depreciable property, or other values considered in arriving at the sale price of \$3, 320, 000. to enable it to pass upon the propriety of the proposed accounting. At the request of the Commission, the Company subsequently furnished the

following breakdown used in determining the sale price. (JA 9a).

	<u>Appraisal</u>	<u>Reduced by</u>	<u>Compromise Figure</u>
Land	\$1,040,965	\$ - - -	\$1,040,965
Real property improvements	2,071,240	150,000	1,921,240
Consequential damage	640,000	315,000	325,000
Machinery & Equipment	176,670	140,000	36,670
Total	<u>\$3,928,875</u>	<u>\$605,000</u>	<u>\$3,323,875</u>
Rounded off	\$3,925,000	\$605,000	\$3,320,000

Based upon this, and other information obtained from the Company and R. L. A., the staff tentatively proposed that the net proceeds from the sale of the property be accounted for as outlined in a letter to the Company under date of April 7, 1959. (JA 33a). The staff's initial proposal, insofar as here pertinent, recommended that the distribution of the net proceeds from the sale of the property, after applying the entire reduction of \$3,875 resulting from the rounding process (shown above) against the proceeds from the depreciable property, and distributing the expenses of the sale in the amount of \$3,756.55 on a pro rata basis between the proceeds from land and depreciable property, should be as follows:

Land	\$1,039,657.72
Real Property improvements	1,915,034.81
Machinery & equipment	36,550.92
Consequential damages	<u>325,000.00</u>
	\$3,316,243.45

Based on the foregoing summary of net proceeds, the accounting initially recommended by the staff in accordance with the Uniform System of Accounts under which the Company operates, is summarized as follows: (JA 10a).

Land

Net proceeds from sale of land	\$1,039,657.72
Less: Original cost of land	<u>89,089.17</u>
Net profit to be credited to earned surplus	<u>\$ 950,568.55</u>

Depreciable Property

Net proceeds from sale of depreciable property to be credited as salvage to the depreciation reserve	\$1,951,585.73
Original cost of depreciable property to be charged to the depreciation reserve	\$1,297,018.77

After certain undisputed modifications and adjustments to the accounting for the proceeds of the sale of the Company's property, (JA 12a, 13a, 19a) the Commission, after due consideration of the factual situation, and the respective positions of its staff and the Company, concluded inter alia, that a departure from the Uniform System of Accounts was justified (JA 16a) and adopted its staffs' alternate proposal that an amount of \$613,661.28 be credited to the depreciation reserve in addition to the \$464,162.78 credited to the reserve under the accounting proposed by the Company. The total

amount ordered to be credited to the reserve from the sale price was the original cost, \$1,077,824.06, of the depreciable property sold, with the difference between this amount and the selling price of \$1,915,034.81, or \$837,210.75, remaining as a credit to earned surplus in addition to the profit of \$950,568.55 on the sale of land (JA 16a, 17a). Item numbered I of the Appendix to Order No. 4577 (JA 21a) shows the required entry to conform to the Commission's prescribed accounting and is the only part of the Commission Order from which the Company appeals. (Note 1, pg. 2, Appellants Br.)

Subsequently, the Company petitioned for reconsideration of the Order (JA 22a) which was denied (JA 43a), and upon appeal to the District Court of the United States for the District of Columbia by the Company, the Court, in a memorandum opinion filed June 10, 1960, held that Order No. 4577 was not unreasonable, arbitrary or capricious and on June 24, 1960 signed an Order granting the Commission's motion for summary judgment and denying the cross-motion of the Company. (JA 28a, 29a)

STATUTE INVOLVED

Act of March 4, 1913 (37 Stat. 974), Sec. 8
Title 43, D. C. Code 1951, (Sec. 310)

"Par. 11. That the Commission shall prescribe the forms of all books, accounts, papers and records required to be kept, and every public

utility is required to keep and render its books, accounts, papers, and records accurately and faithfully in the manner and form prescribed by the commission, and to comply with all directions of the commission relating to such books, accounts, papers and records. In so far as practicable for the purposes of this section, the form prescribed shall be the form accepted by the Interstate Commerce Commission. "

Act of March 4, 1913 (37 Stat. 974), Sec. 8.
Title 43, D. C. Code 1951, (Sec. 314),

"Par. 15. That the Commission shall provide for the examination and audit of all accounts, and all items shall be allocated to the accounts in the manner prescribed by the commission. * * * "

SUMMARY OF ARGUMENT

A utility is entitled to recover from its customers the loss in service value of depreciable property over its life, as measured by the original cost, less salvage, realized upon retirement. Where the sales price upon retirement exceeds the original cost of the property there is no actual loss to be recovered by the utility through depreciation charges to customers.

The Commission, in promulgating the accounting order appealed from, permitted a departure from the Uniform System of Accounts applicable to utilities under its jurisdiction, and such departure benefited the Company. While this is not disputed,

the Company contends the Commission erred in not accepting the Company's version of the extent of the departure from normal accounting procedure. The Company takes the position that extraordinary profits realized from the retirement of depreciable property belong solely to the investors while extraordinary losses occasioned by retirement of property should be borne solely by the fare-paying public. This position ignores the public interest involved in transactions affecting public utilities. The Commission cannot ignore the public interest and the Order appealed from fairly balances the interest of the public and the Company.

The Order appealed from was promulgated by the Commission under authority given the Commission by the Congress. The Order speaks for itself and in the absence of any showing by the Company that it is arbitrary, capricious or unreasonable the decision of the United States District Court for the District of Columbia dismissing the appeal and affirming Order No. 4577 should be affirmed.

ARGUMENT

There Was No Actual Retirement Loss Over The Life Of The Property Involved

I

The Company is entitled, under normal utilities accounting procedure, to recover from its customers, through depreciation, the loss in service value over the life of the property as measured by the original cost of the property less net salvage realized upon retirement. In this case, as may be seen from the statement of the case, the original cost of the depreciable property sold was \$1,077,824.06 and this same property was sold for \$1,915,034.81. Thus, it can be seen that the sales price (or salvage) recovered upon retirement of this property exceeded the original cost by \$837,210.75. Obviously, there was no actual retirement loss over the life of the property and the Company has no bona fide claim upon the depreciation reserve provided by its customers insofar as the retirement of this property is concerned.

II

The Commission's Order Was Reasonable Since It Permitted A Departure From The Uniform System Of Accounts In Favor Of The Company, Yet Considered And Equated The Interest Of The Riding Public.

The Uniform System of Accounts used by the Commission for utilities under its jurisdiction provides that any amount received

from the sale of depreciable property represents the salvage value of such property and is to be credited to the depreciation reserve. The Company contended that the receipt by it from the sale of its depreciable property of approximately \$837,000, more than its original cost was not a normal situation and, therefore, (without the authority of the Commission) departed from the usual retirement accounting procedure whereby all proceeds from the sale of depreciable property are credited to the depreciation reserve.

This unauthorized accounting procedure presented to the Commission the question of whether or not the transaction under consideration was of such a nature as to justify a departure from the Uniform System of Accounts and, if such departure was justified, to determine the extent thereof. The Commission concluded in its Order that a departure from the accounting procedure normally used in retirement transactions was justified in this case.

The Company does not dispute that the Uniform System of Accounts applicable to it provides that amounts received from the sale of depreciable property be credited to the depreciation reserve as salvage. Its position is, that the circumstances of this particular sale of depreciable property justifies a departure from prescribed accounting.

As a consequence, the Company obviously does not dispute the right of the Commission, in this instance, to depart from the accounting procedure it has prescribed for utilities under its jurisdiction.

What the Company does dispute, is the judgment of the Commission in exercising its discretion as to the extent of the departure from normal accounting the Commission would permit. In effect, the Company says that once the Commission permits a departure from prescribed accounting procedures it must necessarily adopt the position of the Company without consideration of other aspects of the depreciation problem or the interest of the fare-paying public.

Let us examine the Company's contentions: The Company contends, that because depreciation has been accrued upon all of its depreciable property, with the authority of the Commission, the particular property herein involved must necessarily have depreciated. It reconciles the fact that the sales price exceeded the original cost of the property (discussed Supra. 1) with the inflationary trend between the date of acquisition and the date of sale. This ignores accepted accounting practices that depreciation loss is computed upon the actual cost of the property as entered upon the books, less the expected salvage, and that the amount charged each year is one years pro rata share of the total amount. Lindheimer v. Illinois Telephone Co., 292 U.S. 151, 167, 54 S.Ct. 658, 78 L.Ed. 1182. Rates of depreciation can at best be only

an educated guess and fairly frequent review and revision is sometimes required. Could it have been anticipated that the salvage (sale price) on the particular property involved in this case would exceed the original cost there could have been no justification for accruing depreciation, which in the last analysis is a charge to customers through the fare box to reimburse the Company for the loss of investment in property dedicated to the public service.

This property was included with other property for which depreciation accrued in the past. However, prior to July 1, 1953 depreciation was accrued on the basis of a composite rate applied to the total investment of the Company in depreciable property, with no segregation of any portion of the depreciation reserve to particular units or classes of property. Effective July 1, 1953 specific depreciation rates were prescribed for the various classes of property (Order 4001) but still no provision was or has been made for segregating the depreciation reserve by particular units or classes of property. Thus, when any portion of the plant is retired it is charged against the reserve in its entirety and net salvage is credited to the reserve in its entirety. No calculation of accrued depreciation is necessary nor is it made. The significance of accruing depreciation on a composite basis

under the "group plan" for depreciation accounting as provided for in the Uniform System of Accounts followed by the Commission is that no portion of the depreciation reserve is associated with any particular unit of property. Accordingly, although the Company has based its accounting for the proceeds of the sale of its depreciable property on the theory that the depreciation reserve reflects accrued depreciation on this particular property in the amount of \$613,661.28, such is not the case. The fact that there is more than sufficient net salvage (sale price) to absorb the full charge for the book loss of the property retired demonstrates that any accruals of depreciation based upon this particular property during its service life were an unneeded burden upon the public for which credit should now be given as ordered by the Commission.

Another contention of the Company is that the Commission had no right to consider the interests of transit customers with respect to anticipated extraordinary retirement losses associated with the abandonment of rail property and conversion to bus operation. The Commission's discussion of this aspect of the Company's contention appears in its Order reproduced, starting at the bottom of page 17a of the Joint Appendix as follows:

"In light of the franchise of the Company requiring a gradual program of conversion from railway to bus operations over a seven-year period from July 24, 1956, we are unable to disassociate the instant transaction from the imminent retirement of all rail property under the mandate contained in the franchise. We cannot ignore the probability that full provision for depreciation will not have been provided when the rail facilities are abandoned and retired by reason of conversion. The Company has consistently taken the position that any retirement loss in this connection should be recovered by charges against the customers, and the staff has heretofore indicated its agreement. However, if the customers are to be required to bear the burden of extraordinary retirement losses incident to the whole conversion program, it appears equitable that they should share, at least to some extent, in extraordinary retirement gains of the nature here under consideration.

The Company takes the position that future losses on disposal of railway property may or may not occur and that known credits should not be used to offset future unknown charges. The Commission agrees that extraordinary retirement losses resulting from the abandonment of railway property prior to the completion of its normal service life cannot be accurately determined at this time. However, we regard extraordinary retirement losses as belonging in the same category as track removal and repaving costs for which provision is presently being made as a charge against the ratepayers on an estimated basis over a ten-year period without objection by the Company. In view of the virtual certainty of future extraordinary retirement losses in connection with conversion, we give little weight to this contention by the Company."

Without belaboring the subject, we note only that the Company has no

objection to projections and estimates of the Commission which the Company feels inures to its benefit.

In addition, appellee feels it ill becomes the Company to complain of an opinion of the Commission, which opinion became fact long prior to the time that the instant appeal was even heard by the District Court.

On November 24, 1959, the Company, in a rate proceeding before the Commission, (the record of which has been certified to the District Court in Cases No. 1439/60 and 1529/60, and is a part of the record before this Court in Case No. 15,999) through its spokesman, originally requested the Commission to provide it with \$5,325,317. of net undepreciated cost of its rail property abandoned or to be abandoned as a result of the conversion provisions of its franchise. It should also be mentioned that the Commission, in entering its order and opinion in the aforementioned proceeding (also part of the record), made an additional provision for depreciation in the amount of \$2,530,092. to permit the Company to recover the undepreciated costs of that portion of its rail facilities abandoned on January 3, 1960. *

* For the convenience of the Court, appellee includes as an appendix to its brief, the pertinent portion of the testimony, exhibits and opinion in the proceeding dealing with the undepreciated cost of rail property.

The Company thus blows hot and cold. With a heads, I win; tails, you lose; attitude, it takes the position that extraordinary profits realized from retirement of depreciable property belongs solely to investors, while extraordinary losses occasioned by retirement of property should be saddled solely on the fare-paying public.

Finally it appears to be the contention of the Company that the Commission is in some way obligated to compensate it for any inflationary trend between the dates of acquisition of the property involved and its sale. Interwoven in the Company's contention with respect to inflation is a discussion of the sale price being based upon reproduction cost. The short and simple answer to the Company's claim that it should be shielded from the effects of inflation is that this Commission has never attempted to compensate for a decline in the value of the dollar in providing for depreciation. Insofar as appellee can determine no other regulatory body has based estimated depreciation upon other than original cost less salvage. Though some jurisdictions permit or require consideration of reproduction cost in rate base, the Company has not pointed out, nor has appellee found any jurisdiction using reproduction cost as a basis for depreciation. Whatever the basis for the selling price of the property involved, and whatever the extent of the inflationary trend the fact remains that the proceeds from the sale

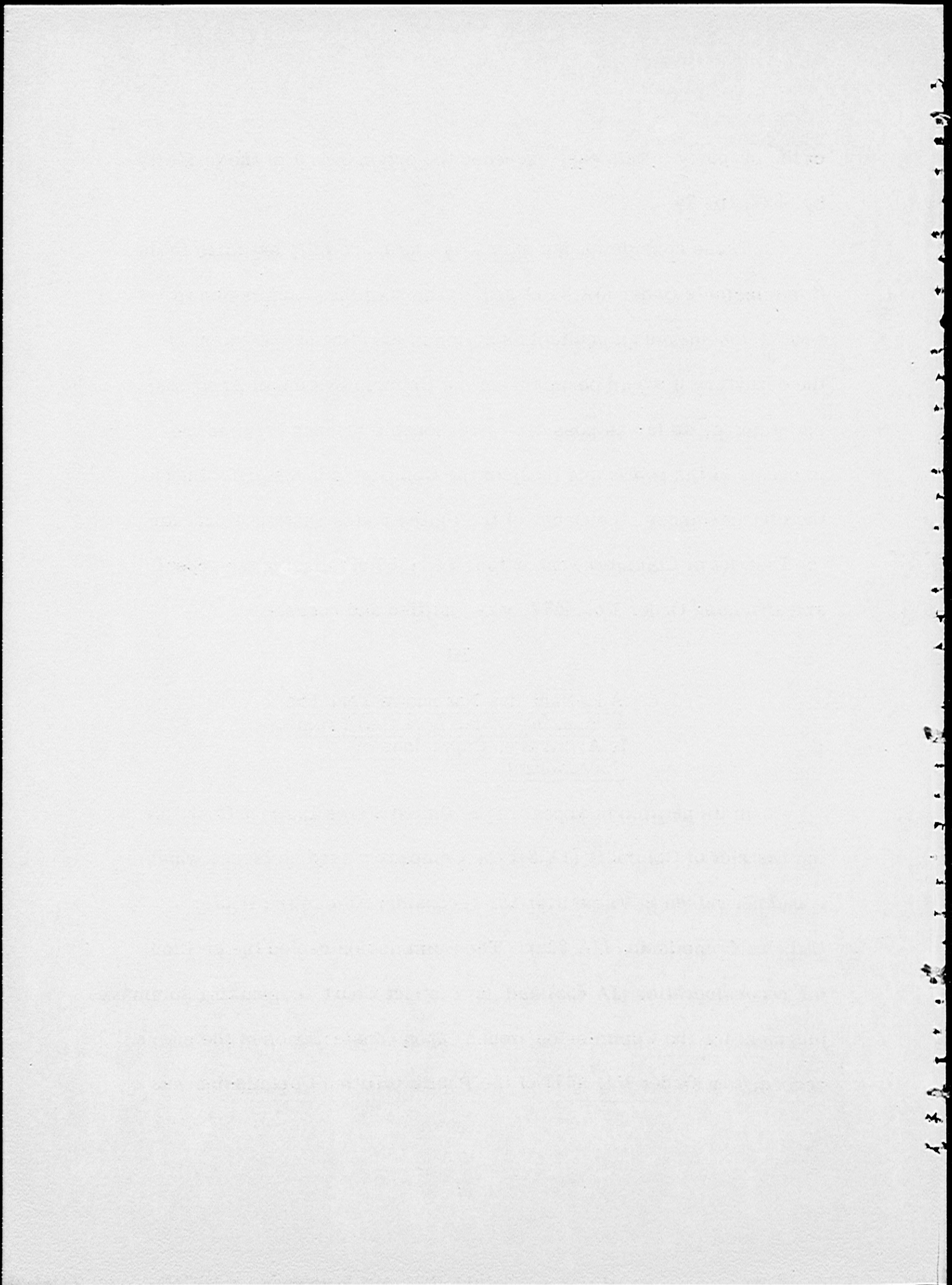
of the property in this case exceeded the original cost of the property by \$837,210.75.

These considerations inter alia, as more fully set forth in the Commission's Order (JA 8a et seq.) prompted the Commission to what it considered an equitable solution in arriving at the extent of the departure it would permit from the Uniform System of Accounts; maintaining, as far as possible, a reasonable balance between the interests of the public and those of the Company's investors. Under the circumstances, the Order of the United States District Court for the District of Columbia, dated June 24, 1960 dismissing the appeal and affirming Order No. 4577, was justified and correct.

III

Appellant Has Not Shown That The
Accounting Order Appealed From
Is Arbitrary, Capricious or
Unreasonable.

In its petition of appeal to the United States District Court for the District of Columbia (JA 3a) the Company raised no issues which it had not raised in its petition for reconsideration to the Public Utilities Commission (JA 22a). The Commission denied the petition for reconsideration (JA 43a) and the District Court, in granting summary judgment for the Commission, found, upon consideration of the entire record, that Order No. 4577 of the Public Utilities Commission was



from the Congress is Par. 11 (Sec. 310), which provides:

"That the commission shall prescribe the forms of all books, accounts, papers, and records required to be kept, and every public utility is required to keep and render its books, accounts, papers, and records accurately and faithfully in the manner and form prescribed by the commission, and to comply with all directions of the commission relating to such books, accounts, papers and records. In so far as practicable for the purposes of this section, the form prescribed shall be the form accepted by the Interstate Commerce Commission."

and Par. 15 (Sec. 314), which provides inter alia:

"That the commission shall provide for the examination and audit of all accounts, and all items shall be allocated to the accounts in the manner prescribed by the commission. ** "

The Act (supra) as a whole, makes it abundantly clear that the Commission is the administrative body to whose judgment and discretion Congress has committed the determination of accounting matters. When such determinations have been made, they will not be set aside unless they are clearly unreasonable, arbitrary, or capricious. Where accounting matters are committed to administrative bodies, the courts have consistently refused to determine accounting practices or interfere with accounting requirements unless the administrative body has "plainly adopted an obviously arbitrary plan." Northwestern Electric Co. v. F. P. C., 321 U. S. 119, 124, 64 S. Ct. 451, 88 L. Ed. 596. Arkansas Power and Light Co. v. F. P. C., 87 U. S. App. D. C.

385, 185 Fed. 2d. 751, (Cert. d. 341 U. S. 909); Alabama Power Co. v. F. P. C., 75 U. S. App. D. C. 315, 128 Fed. 2d. 280 (Cert d. 317 U. S. 652); Clarion River Power Co. v. Smith, 61 App. D. C. 186, 59 Fed. 2d. 861, (Cert. d. 287 U. S. 639). In attacks upon administrative accounting orders, the courts have said that even though they were in disagreement with the regulatory agency "as to the wisdom and the propriety of the order, we are without power to usurp its discretion and substitute our own". Norfolk & Western R. R. Co. v. U. S. 287 U. S. 134, 141, 53 S. Ct. 52, 77 L. Ed. 218; Kansas City So. Ry. v. U. S. 231 U. S. 423, 444, 456, 34 S. Ct. 125, 58 L. Ed. 296; American Tel. & Tel. Co. v. U. S., 299 U. S. 232, 236-237, 57 S. Ct. 170, 81 L. Ed. 178.

In view of the law applicable to a situation of this kind, the position of the Company on this appeal cannot be supported. The unsupported allegations of error made represent nothing more than a difference of opinion with that of the Commission expressed in the Accounting Order appealed from. In the absence of any factual showing that the findings of the Commission are unreasonable, arbitrary or capricious, review by the Court is limited to questions of law. General statements by the Company disagreeing with the conclusions reached by the Commission are not sufficient to show that

the matters complained of are erroneous, and constitute no legal basis for invalidating an Accounting Order promulgated by the Commission pursuant to its statutory authority.

CONCLUSION

The Order of the United States District Court for the District of Columbia dismissing the appeal and affirming Order No. 4577 of the Public Utilities Commission of the District of Columbia dated June 24, 1960 should be affirmed.

Respectfully submitted,

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General Counsel

GEORGE F. DONNELLA
Counsel

ANDREW G. CONLYN
Counsel

Attorneys for Appellee
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APPENDIX

I N D E X

SUBJECT INDEX

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Excerpts From Transcript of Proceedings

90

JAMES H. FLANAGAN

resumed the stand and, having been previously duly sworn, was examined and testified further as follows:

DIRECT EXAMINATION (Continued)

By Mr. Spear:

*

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*

96 Q Mr. Flanagan, will you explain how you arrived at the amount of depreciation shown on Exhibit 10 and in Line 11, I believe? A This item is of the utmost importance and requires a considerable amount of discussion.

Due to the provisions of our franchise contained in Public Law 757, and in conformity with the repeated urgings of the Public Utilities Commission, we have proceeded with the conversion from streetcar operations to bus operations. As we have already pointed out, one phase of this conversion was completed in 1958 and further substantial conversion is contemplated to be completed almost immediately.

Testimony has already been introduced in this record to show that over 60 per cent of the single track feet of rails will be abandoned. This calls for full realization of the fact that the character of the investment of the company in transit facilities has changed. It calls for an evaluation of the tremendous

loss of property value that has already been realized. It calls for plans to provide for the recovery of that portion of the investment in property purchased for the purpose of devoting it to public service, which has not already been recovered through provisions for depreciation.

Schedule 4 attached to this Exhibit Number 10 shows on Page 1 the computation of the amount of additional annual depreciation, \$654,358, necessary to comply with requirements that the original cost investment in property devoted to public service should be recouped through provisions for depreciation.

BY MR. SPEAR:

Q Mr. Flanagan, when you talk of Schedule 4, I don't believe the notation "Schedule 4" is on the page to which you refer. Are you referring to the next to the last page of Exhibit Number 10? A Yes. The last two pages attached to Exhibit Number 10 are considered to be and should be marked Exhibit Number 4.

BY MR. SPEAR:

Q Schedule Number 4? A Schedule Number 4.

BY MR. SPEAR:

Q And those are the pages that start "Statement of Depreciation at Current, Existing Rates, September 30, 1959? A That is right.

BY MR. SPEAR:

Q And the second statement is entitled "Statement of Undepreciated

Cost of Rail Properties, September 30, 1959"? A Yes.

BY MR. SPEAR:

Q All right. Will you continue your explanation? A Page 2 of Schedule 4 shows how the depreciation provisions necessary to recover the net undepreciated cost of rail property over future annual periods was calculated. In the first column of this page, there is shown the original cost of streetcars and other rail property which will be abandoned as conversion to bus service takes place. As required by the company's franchise, total conversion must be accomplished by August 15th, 1963.

I call attention to the amount reflected in that first column.

We are in the process of abandoning property which at its original cost was \$23,595,539.

The second column shows the amount of depreciation which has been accumulated through the years to provide for the recovery of the original cost of the rail property. These calculations are predicated upon a depreciation study prepared in 1954 by Mr. J. L. Ingoldsby, a member of the engineering staff of the Public Utilities Commission, and brought up to date to September 30, 1959 by us.

From that column, it will be noted that the amount accumulated is only \$17,711,404.

The third column shows that there remains a balance of \$5,884,134 of the original cost which has not been depreciated, and for which provision

must now be made. After providing for the estimated salvage value of all this property, or \$558,817, we arrive at the amount of \$5,325,317 as the net undepreciated cost of rail property as at September 30, 1959.

There remains 43-1/2 months from January 1, 1960 of the period of seven years stipulated in the company's franchise as the period within which conversion must be completed. The company has provided in its projections of future operations for the recovery of the net undepreciated cost of \$5,325,317 over this period of 43-1/2 months. The result is a monthly charge to depreciation of \$122,421, or an annual charge of \$1,469,053. The establishment of a provision as explained above will, of course, necessitate the discontinuance of the regular annual provision for depreciation on the property which is to be abandoned. As shown on Page 1 of Schedule 4, this annual provision amounts to \$814,695. Thus, the additional depreciation becomes the difference between the two figures, or \$654,358. Normal depreciation on buses and other property will continue as at present.

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STATEMENT OF UNDEPRECIATED COST OF RAIL PROPERTIES

September 30, 1959

	Original Cost	Accumulated Depreciation (Note 3)	Undepreciated Original Cost	Estimated Salvage (Note 1)
Passenger street car	\$ 8,508,759	\$ 5,686,365	\$2,822,394	\$255,262
Rail service equipment	147,238	110,218	37,020	2,945
Track and line	12,555,795	10,375,589	2,180,206	None-Note 2
Duct system	839,836	686,574	153,262	-
Low tension cables	1,117,070	594,068	523,002	279,268
Substation equipment	<u>426,840</u>	<u>258,590</u>	<u>168,250</u>	<u>21,342</u>
	\$23,595,538	\$17,711,404	\$5,884,134	\$558,817
			<u>-558,817</u>	
Net undepreciated cost, September 30, 1959			<u>\$5,325,317</u>	

Depreciation per month, to recover net undepreciated cost over
future annual periods (January 1, 1960 to August 15, 1963,
43.5 months) as required by franchise

\$122,421.08

Note 1: Salvage credits conform to estimates made by P. U. C. Consultant, J. L. Ingoldsby in property study of 1954.

Note 2: Estimated salvage credits on track and line have been availed of in the development of the provision for track removal and repairing and, hence, are not available as a salvage credit in this study.

Note 3: Accumulations of depreciation by classes of property have been computed using the 1954 property study of J. L. Ingoldsby, P. U. C. Consultant, as a starting point. Depreciation accumulations since that study, net of retirements, are herein reflected.

PUBLIC UTILITIES COMMISSION OF THE DISTRICT OF COLUMBIA

March 31, 1960

IN THE MATTER OF)

Petition of D. C. Transit System, Inc.)
For Change in Schedule of Rates.)

P. U. C. No. 3628
Formal Case No. 471

OPINION IN SUPPORT OF
FINDINGS, CONCLUSIONS, AND ORDER
PROMULGATED MARCH 3, 1960
(Order No. 4631)

* * * * *

As shown by Company Exhibit No. 10-A, the estimated net undepreciated cost of rail facilities as of December 31, 1959, amounts to \$5,121,644, and it was proposed by the Company witness that this amount be fully recovered over the remaining 43.5 months of the conversion period from January 1, 1960 through August 15, 1963. This would require a monthly provision of \$117,738.94 instead of the present provision of \$67,891.25 under rates prescribed by this Commission, an increase of \$49,847.69 per month or \$598,172 on an annual basis.

The staff witness agreed with the Company estimate of net undepreciated cost as of December 31, 1959, in the amount of \$5,121,644, and that the Company is entitled to recover this amount over some future period. It was his position, however, that to make provision for recovery of the entire amount over the remaining 43.5 months of the conversion period would place too heavy a burden on the customers during this period. It was his proposal that we now

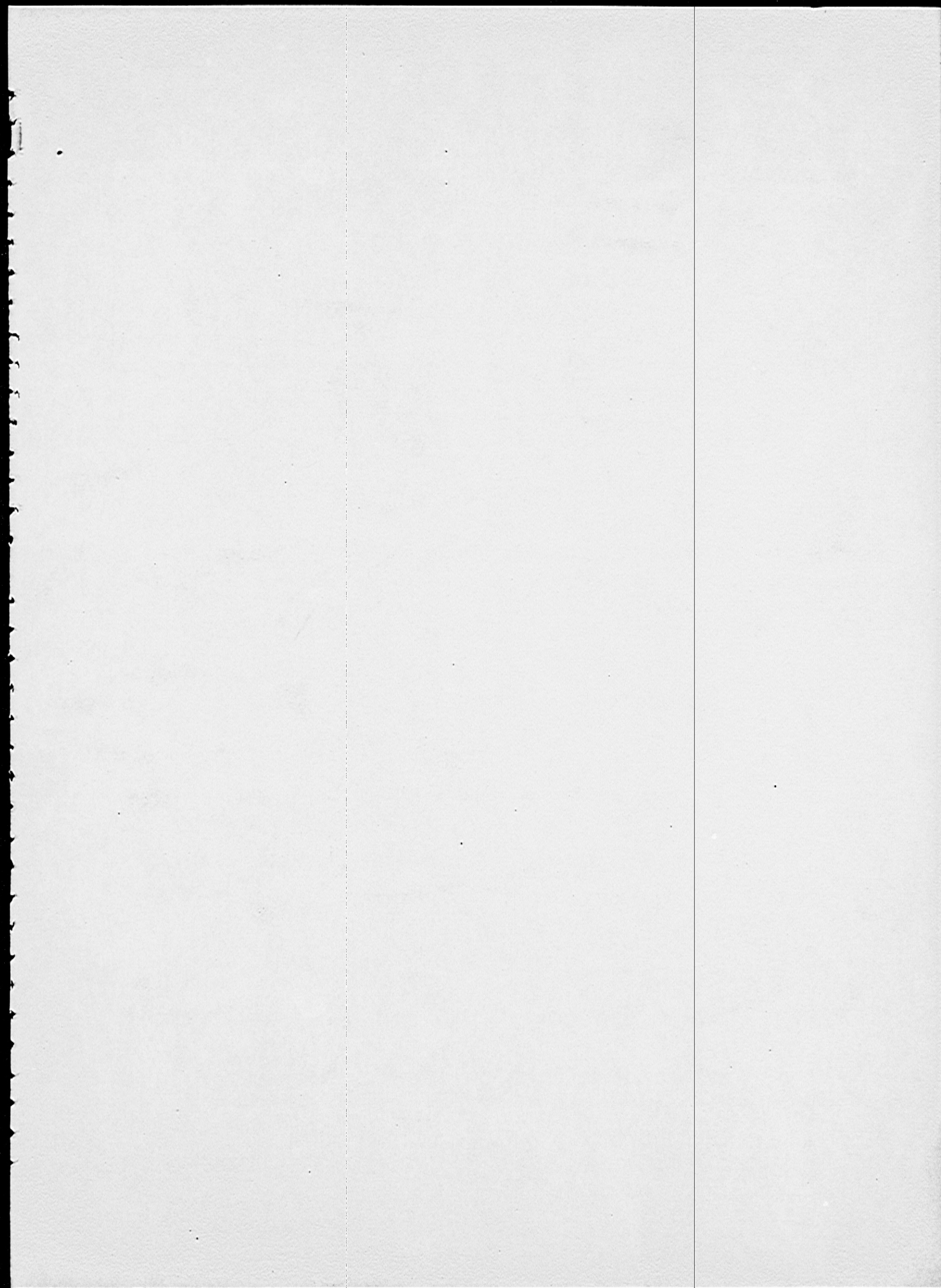
make provision only for that portion of the undepreciated cost that is associated with the track facilities that were abandoned on January 3, 1960. Using a factor of 49.40% based on the relation of the single track footage of rail facilities abandoned on January 3, 1960, to total track footage prior to that date, the undepreciated cost of these facilities would amount to \$2,530,092. On this basis, additional provision of \$295,500 per annum would be required over and above the provision presently being made on total rail facilities as of December 31, 1959. His estimate of depreciation for the future annual period in the amount of \$2,691,015 reflects this additional provision of \$295,500, instead of the Company proposal of \$598,172.

With respect to the undepreciated cost related to the remaining track facilities, it was the recommendation of the staff witness that provision should be made for recovering these costs in the light of conditions existing at the time these facilities are actually abandoned. He directed attention to the fact that the depreciation study used as a basis for determining the estimated undepreciated cost of rail facilities as of December 31, 1959, was completed in the early part of 1953, and that it is quite possible that a current study might result in a somewhat different determination of the amount of unrecovered depreciation assignable to these track facilities. The record also shows that under the group method of depreciation provided for in our Order No. 4001, approximately \$1,200,000 of depreciation over and above original cost has been accrued on buses that have exceeded their estimated normal service life

of 14 years. The staff witness proposed that any excess accruals applicable to over-age buses might well be applied as a partial offset to any unrecovered depreciation related to rail facilities that might be disclosed by a depreciation study.

It is the opinion of the Commission that until such time as a new depreciation study is made, and until we have had sufficient experience with the actual cost of track removal and repaving work to test the adequacy or inadequacy of the present provision for track removal, the additional provision of \$295,500 recommended by the staff witness is as far as the Commission should go at this time in making separate provision for extraordinary retirement loss related to track facilities. Numerous precedents can be found where commissions have provided for recovering extraordinary retirement losses resulting from obsolescence over a reasonable period in the future.

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REPLY BRIEF FOR APPELLANT

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 15,967

D. C. TRANSIT SYSTEM, INC., APPELLANT

v.

PUBLIC UTILITIES COMMISSION OF THE
DISTRICT OF COLUMBIA, APPELLEE

Appeal from a Decision of the United States District Court
for the District of Columbia

United States Court of Appeals
For the
District of Columbia Circuit

FILED

JAN 31 1961

Joseph W. Stewart

CLERK

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3600 M Street, N.W.
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UNITED STATES COURT OF APPEALS
For The District of Columbia Circuit

No. 15,967

D. C. TRANSIT SYSTEM, INC.

Appellant,

v.

PUBLIC UTILITIES COMMISSION

Appellee.

Appeal From The United States District Court
For The District Of Columbia

REPLY BRIEF FOR APPELLANT D. C. TRANSIT SYSTEM, INC.

INTRODUCTION

This is not an appeal from a finding of fact or from an order involving a rule making function within the traditional discretionary power of a regulatory agency. Rather, this is an appeal involving the basic legal proposition of whether a public utility is entitled, as a matter of law, to be compensated for loss of service life of its property resulting from wear and tear.

The Briefs of Transit and of the Commission agree on the legal point that if the accounting order of the Commission involved herein is found to have been "unreasonable" it may be reviewed and modified by this Court.

The Briefs also agree on the first important substantive point herein, i.e. that the sale in 1959 by Transit of its Fourth Street Shops and Southern Carhouse, some parts of which were acquired as early as 1915, to the District of Columbia Redevelopment Land Agency under threat of Condemnation for a sum considerably in excess of the original cost of the properties, was such a transaction as justified departure from the customary Uniform System of Accounts in accounting for the transaction.

The Briefs disagree, however, on the matter of the account to which a certain part of the proceeds of the sale should be credited. More specifically, whereas Transit credited its depreciation reserve accounts with \$464,163 the Commission has ordered that the credit should be increased by an additional \$613,661, bringing the total credit in 1959 to \$1,077,824. (Adjustment Entry No. 1) The additional \$613,661 credit represents a duplication of a similar amount credited by Transit to its depreciation reserve by annual depreciation provisions over each of the years of service life of the property. If the duplicate or second \$613,661 is credited to the

reserve as urged by the Commission herein then the reserve would contain depreciation credits of approximately 150% of the original cost of the properties.

Transit differs with the Commission on that portion of its Order which would credit the second \$613,661 to the depreciation reserves (Adjustment Entry No. 1).

The Commission's Brief makes two points both of which it must prove in order to sustain its contention that Adjustment Entry No. 1 was "reasonable". If the views of Transit are adopted on either of these two points, then Adjustment Entry No. 1 of the Commission's Order was in error.

SUPPLEMENTARY ARGUMENT

I

The Commission Erred in Concluding That There Was No Loss of Service Life Sufficient To Justify Depreciation Accruals During The Service Life of the Property.

The first major point of the Commission's Brief is that, because the sales price of the property in 1959 exceeded its original cost, which in part dated back to the year 1915, there was no loss of service life or service value during the intervening years of service use. In this basic premise the Commission is in error for the reasons pointed out in Transit's Brief (pages 15-19).

Bearing in mind that the depreciation accruals over the service life of the property were accrued pursuant to Commission orders then in effect, the Commission's Adjustment Entry No. 1 herein amounts to a reversal of position.

This reversal of position indicates that the Commission is blowing both hot and cold as it suits its convenience. Thus, during the years the property was in use, the Commission ordered an annual depreciation accrual representing the loss or consumption of service value in each such year. Now that the property is sold, the Commission reverses position and argues that the accruals which they previously directed should never have been made; that having been erroneously accrued, they now should, in effect, be confiscated and a second duplicate credit of \$613,661 should be made out of the proceeds of the 1959 sale.

The fallacy in the argument of the Commission can best be seen in the following quotation from the first paragraph of its "Summary of Argument" (Appellee's Brief, p.7):

"A utility is entitled to recover from its customers the loss in service value of depreciable property over its life, as measured by original cost, less salvage, realized upon retirement. Where the sales price upon retirement exceeds the original cost of the property there is no actual loss to be recovered by the utility through depreciation charges to customers." (Underlining supplied).

If by "actual loss" the Commission means there has been no loss in numbers of dollars between 1959 and 1915 because of inflation, then, of course, the Commission is correct in its mathematical comparison. But, if by "actual loss" the Commission is trying to claim that in using the property over many years there was no loss in usable value or service value, then the Commission has grievously erred. It is clear that loss in usable value or service value does automatically take place and is coincident with wear and tear through usage.

The Commission has erred gravely in arguing that because the dollar price at the time of sale in 1959 exceeded original cost dating back in part to 1915, there was no wear and tear and hence no loss of usable value notwithstanding usage and consumption of service life during the intervening years.

The Commission's argument means that whenever inflation, even during a given year, results in a property having a greater dollar value at the end of the year than it had at the beginning of the year, then the increased number of dollars of value represented by the year's inflation, must be subtracted from the depreciation accrual for that year before the income account and property can be charged with any consumption or usage of service life or service value in that year. This argument of the Commission is patently fallacious, as is

obvious if one considers what would happen to such a rule in case of deflation during a given year. Under this theory, in times of deflation, presumably, annual depreciation provisions would have to be increased to compensate the utility for loss in dollar value resulting from deflation in any given year.

The reason the Commission has erred is that, in determining whether there is loss of service value, the Commission is comparing apples and oranges. The only way to determine whether there is a loss of service value is to compare the real value of the property at the beginning of a period of service usage with its real value at the end of the period of service usage. If the property has been partly consumed or used in that period, there is a loss of service usage or service value, regardless of what inflation or deflation may do to the number of dollars represented by the property. If inflation causes the dollar value at the end of the period to be a greater number of dollars than at the beginning of the period, each dollar necessarily will be worth less. Conversely, the result will be opposite in the case of deflation. But one conclusion will emerge unalterably from either inflation or deflation, namely, that regardless of what happens to the number of dollars in the case of inflation or deflation, usage of the property repre-

sents consumption of the property for which the owner is entitled to compensation in the form of a depreciation accrual. Here, the Commission argues that where the sales price of a particular unit of property exceeds its original cost there can be no loss of service life to the utility. But, the Commission's argument fails to recognize that, although inflation may have caused the property at the time of sale to have a higher price than its original cost, that some inflation would have caused a still higher sales price were it not for the loss of service life resulting from wear and tear. It is for this loss of service life resulting from wear and tear that a public utility must be compensated, even where inflation makes the property worth more dollars.

The Commission has further confused the picture on this appeal by claiming that Transit's position represents a replacement-value depreciation argument. This is just the opposite of the truth. Transit is here arguing to preserve the depreciation it has accumulated over the years on an original-cost base.

A careful analysis shows it is the Commission that is being misled by replacement-value accounting. Thus, at the time of sale in 1959, Transit, in accordance with

standard practice, brought its depreciation reserve to 100% of its original cost before writing off the properties retired. But if the Commission's Adjustment Entry No. 1 were adopted, the reserve would approximate 150% of the original cost, and all of this excess would be the result of the Commission relying on the replacement value of the property as the basis for increasing the reserve to 150% of original cost.

On this point, then, the Commission is once again blowing hot and cold. Generally, it opposes depreciation based on replacement value. In this case, however, it uses the fact that the replacement value exceeds the original cost to justify increasing the depreciation reserve to 150% of original cost. In this the Commission is clearly in error.

Finally, it is necessary to direct the Court's attention to another example of inconsistency in the position taken by the Commission. At page 13 of its Brief the Commission argues that "*** although the Company has based its accounting for the proceeds of the sale of its depreciable property on the theory that the depreciation reserve reflects accrued depreciation on this particular property in the amount of \$613,661.28, such is not the case." The Commission bases its argument on the theory that under

the group plan of depreciation accounting "* * * no portion of the depreciation reserve is associated with any particular unit of property." (Appellee's Brief pp 12-13). This argument is inconsistent with the position taken by the Commission in its order wherein it is recognized that certain portions of the reserve may be associated with particular units of property. In its order, the Commission justified its departure from the Uniform System of Accounts by associating the depreciation reserve with the particular property at issue herein. In its Discussion and Conclusions the order states the following:

"We believe that the fact that application of normal accounting procedures would build the reserve for depreciation to a point where it would contain approximately 80 per cent more than is necessary to retire 100 per cent of the original cost of these properties justifies a departure from the Uniform System of Accounts. We so find and conclude."
(J.A. 15a - 16a).

Needless to say, this is a clear example of conflict between the position taken by the Commission's Brief and that expressed in its order. It demonstrates, as Transit contends, that the depreciation reserve can and must be related to the property involved herein.

II

The Commission Erred in Concluding That The Depreciation Reserve Required Building-Up Out Of The Proceeds Of The 1959 Sale Because The Reserve Was Insufficient To Provide For Future Anticipated Losses From Impending Conversion.

The effort of the Commission to build up Transit's depreciation reserve to an amount equivalent to 150% of the original cost of the property is justified by the Commission's second erroneous premise, i.e. that the depreciation reserve required building-up out of the proceeds of the 1959 sale because the reserve was insufficient to provide for future anticipated losses from impending conversion of street railways to bus operations.

This is the second principal contention of the Commission, and its second error.

Here again the Commission is blowing both hot and cold as it proves expedient. Thus, whereas to justify its accounting entry herein, the Commission argues that the overall depreciation reserve is deficient, in a current rate proceeding before it, the Commission has found the opposite to be true.

In Order No. 4735 dated January 18, 1961,^{1]} the

^{1]}The pertinent parts of the Order are attached hereto as Appendix A for ready reference.

Commission denied Transit a rate increase primarily on the ground that its depreciation reserve is excessive, and that accordingly the annual depreciation provision should be reduced to provide the Company the added income sought in the rate proceeding. Briefly stated, the Commission found an excess in the depreciation reserve accounts of \$2,414,638, which it found in that rate proceeding to be more than sufficient to absorb any anticipated losses from the impending conversion from street railways to bus operations. In addition to earmarking the \$2,414,638 for that purpose, the Commission reduced Transit's annual depreciation provision by a substantial amount.

Here again then, the Commission is blowing hot and cold in a way that repudiates the reasoning that the depreciation reserve should be increased out of the proceeds of the 1959 R. L. A. sale allegedly to provide for anticipated losses from conversion.

There is no need for increasing the reserve in the light of the findings in Order No. 4735, all of the background for which was available to the Commission when it ordered Adjustment Entry No. 1 herein. Moreover, there is no legal basis for interrelating the 1959 R. L. A. sale under threat of redevelopment condemnation with prospective conversion of street railways to bus operations. The two matters are strictly unrelated.

CONCLUSION

The Commission must prevail on both of the two points discussed herein. If the views urged by Transit under either point are adopted by the Court, then Adjustment Entry No. 1 of the Commission's order was "unreasonable" and in error.

For all of the above reasons and for the reasons expressed in its Brief herein, Transit respectfully urges this Court to vacate and set aside Adjustment Entry No. 1 of the Commission's Order No. 4577.

Respectfully submitted,

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Owen J. Malone

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Washington 7, D. C.

APPENDIX "A"

PUBLIC UTILITIES COMMISSION
OF THE DISTRICT OF COLUMBIA

Order No. 4735

January 18, 1961

In The Matter Of	}	P.U.C. No. 3640 Formal Case No. 474
Petition of D. C. Transit System, Inc.		
For Change in Schedule of Rates		

* * *

Findings and Conclusions

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13. That the group method of depreciation for buses, heretofore used, has resulted in an excess accrual of depreciation, based upon the investment in 1,060 buses still in service, in the amount of \$2,414,638.

14. That the excess depreciation accrued on buses in the amount of \$2,414,638 will be more than sufficient to meet anticipated retirement losses on the remaining rail facilities and should be used for this purpose, with the remainder to be applied, if needed, to other property.

15. The excess depreciation accrual of \$2,414,638, arising from bus property, will eliminate any present need to increase the annual rates of depreciation on other than bus property.

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By the Commission:

A True Copy

Norman B. Belt
Executive Secretary

